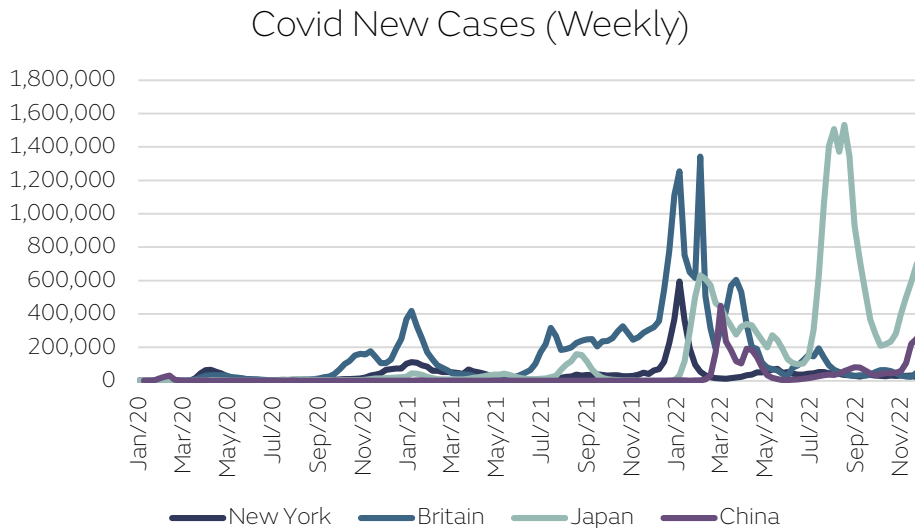


December 2022: Season's Greetings, It's not a New Year

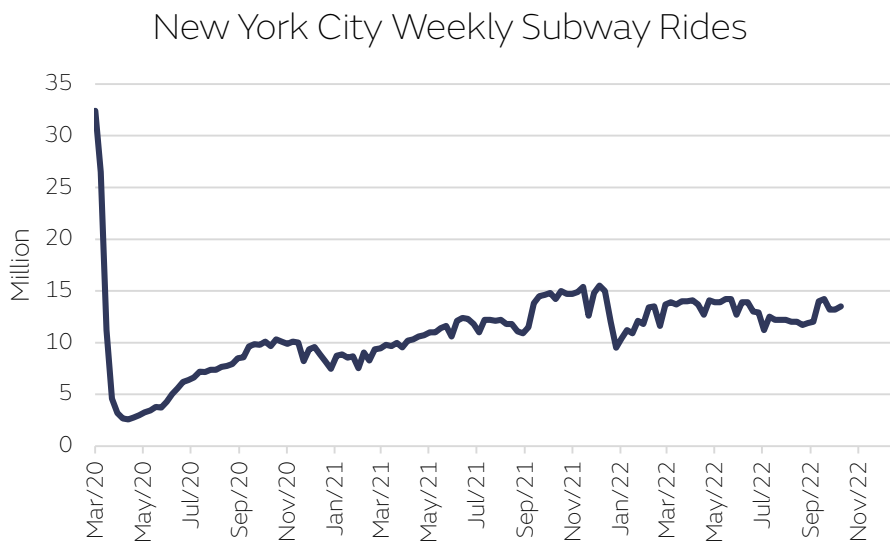
As we wrap up 2022, all eyes turn ahead to prospects for 2023. While what we all want for Christmas is COVID-19 to be behind us, globally we are not yet out of the woods.



Source: Bloomberg

Thus while the notion that the COVID pandemic is “over”¹ may be premature, the idea that things are going back to normal is plainly wrong. Firstly, financial markets don’t “go back” to anything on the simple basis that we invest going forward. Secondly there are clear indications of secular change that suggest a medium term (18 mo – 3 year) outlook will be more appropriate than simple New Year plans.

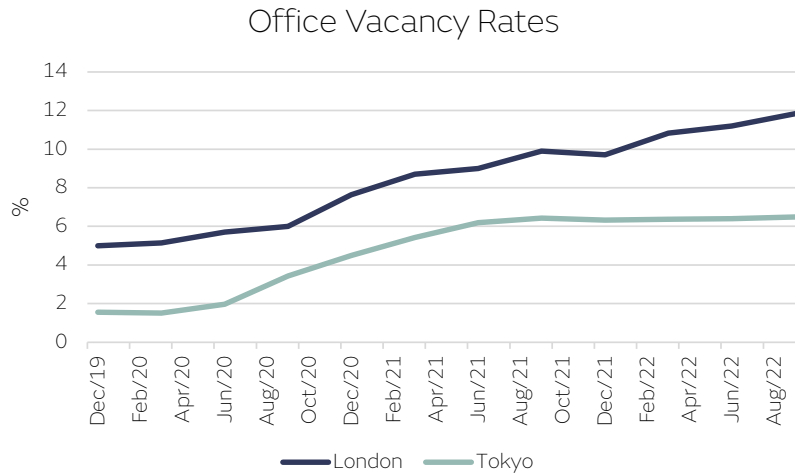
We are living our lives differently. How and where we work has changed. New Yorkers are not returning to ride the subway.



Source: MTA

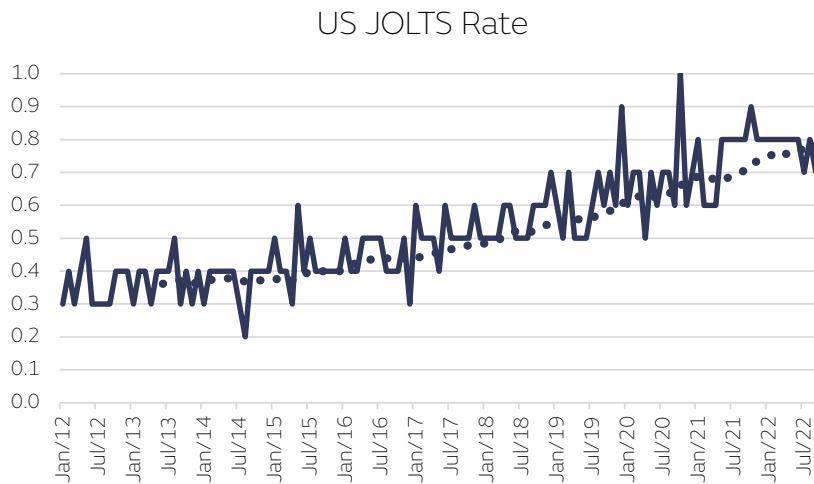
¹<https://www.cbsnews.com/news/president-joe-biden-60-minutes-interview-transcript-2022-09-18/>

In London and Tokyo office vacancy rates have risen and remain elevated above pre-pandemic levels.



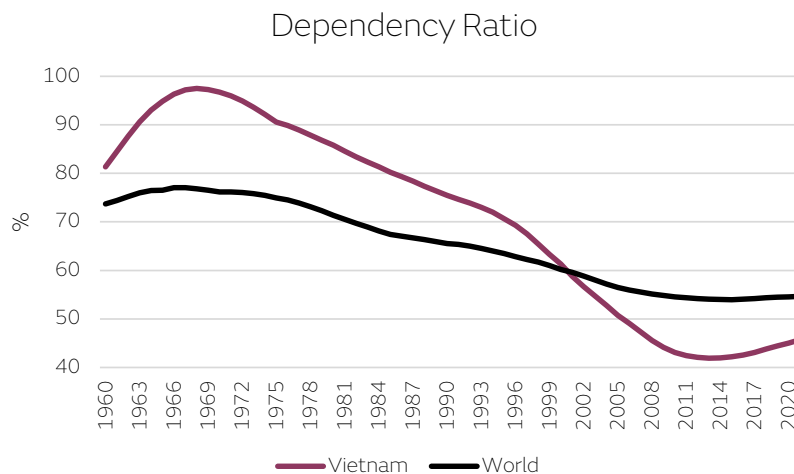
Source: Bloomberg

At the same time employees are quitting their jobs at 10-year quarterly average record levels.



Source: Bureau of Labor Statistics

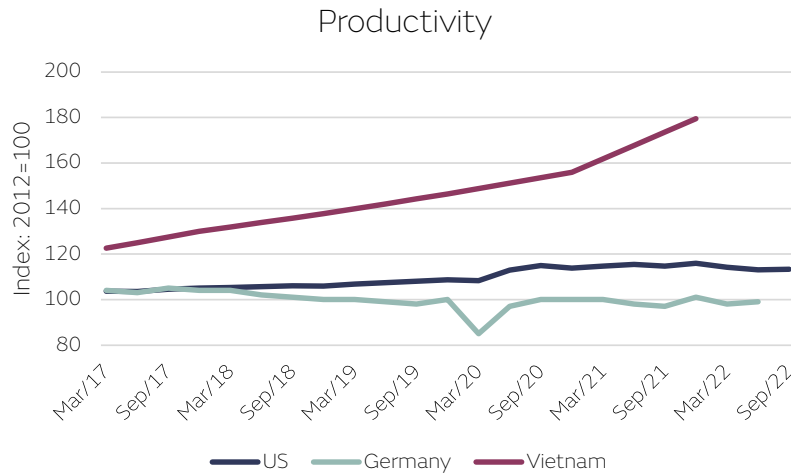
This all suggests a structural reversal of employer power from previous decades and is evidenced by increased instances of industrial action. We observe several other secular shifts. 1) Globally, dependency ratios² are rising even in those markets (e.g. Vietnam) which have seen some of the most substantive declines.



Source: The World Bank

² The number of economically dependent population per 100 economically productive population

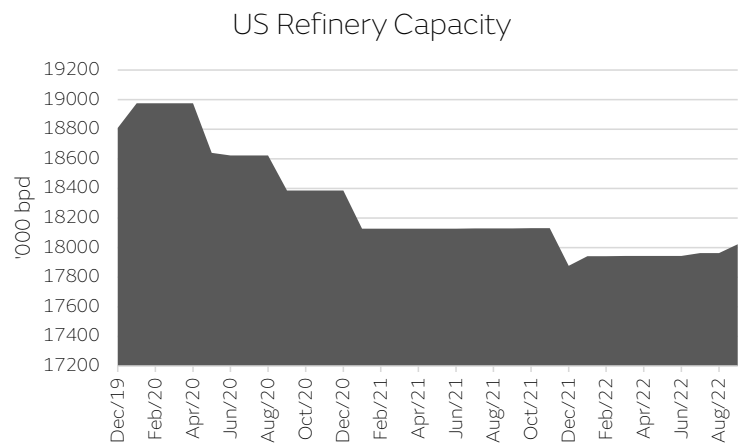
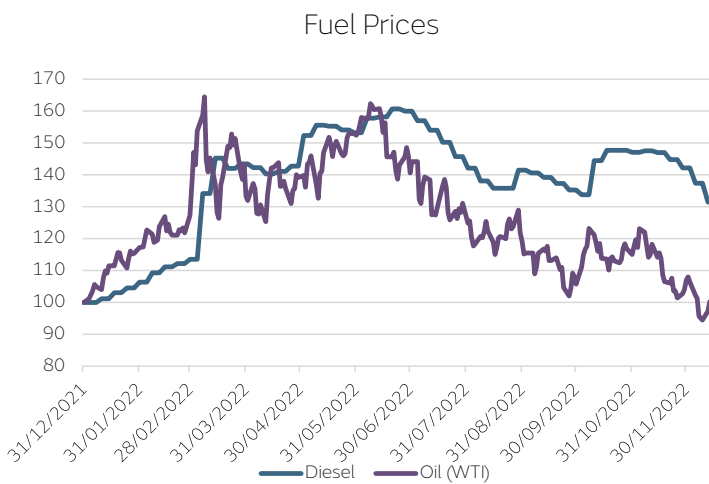
2) While productivity in emerging markets, such as Vietnam, continues to expand, productivity in “mature” industrialised economies appears to be peaking.



Source: Bureau of Labor Statistics, OECD, VEPR

3) The push for domestic supply of essential goods (re- and friend-shoring) continues to gain momentum and, based on Reshoring Initiative³ data, is at record levels.

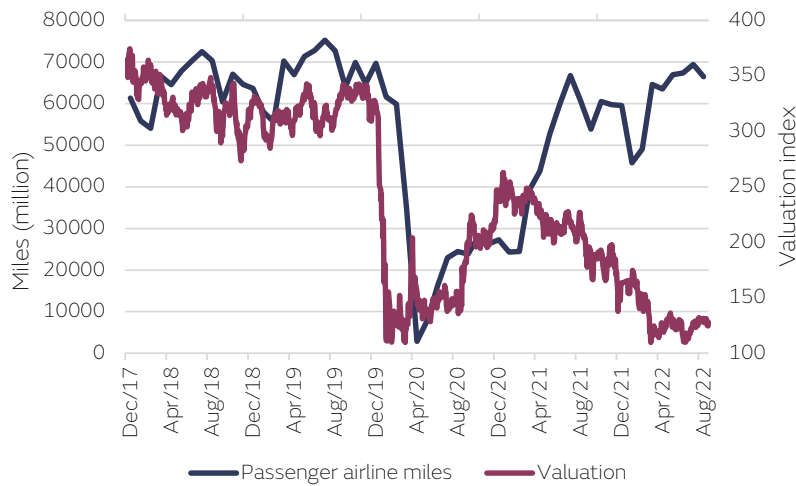
Besides these secular shifts there are other long term expectations that drive outcomes. For example the long term expectation of a transition away from fossil fuels restrains investment in new refinery capacity. Accordingly the recovery in demand for end product, such as diesel or jet fuel, means higher product prices regardless of the amount of raw material (oil) produced. This has been evident over the course of the year and will remain persistent so long as production capacity continues to decline.



Source: US Department of Energy

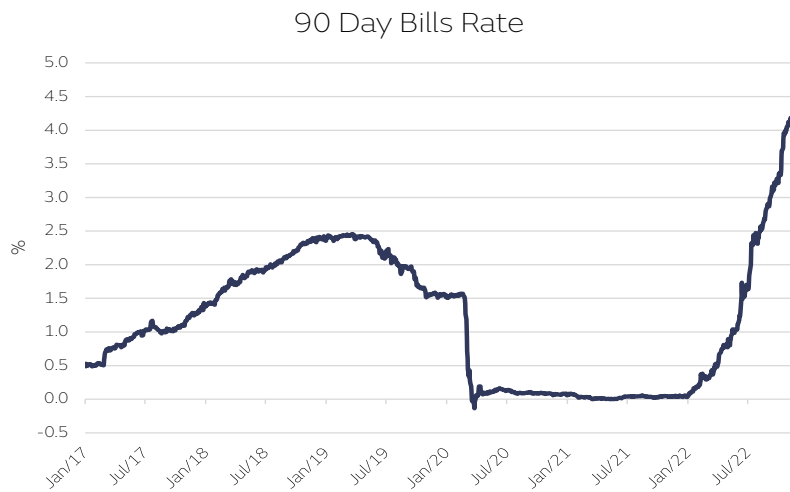
Thus structural shifts to higher prices mean that an apparent resumption of activity doesn't mean equity valuations follow. So while Americans have returned to the skies, the valuation of the airlines (on an equal weighted peer basis) remains weak and way below pre-pandemic levels.

³ <https://www.qualitymag.com/articles/97116-reshoring-initiative-1h-2022-data-report-multiple-supply-chain-risks-accelerate-reshoring>



Source: US Department of Transportation and Bloomberg

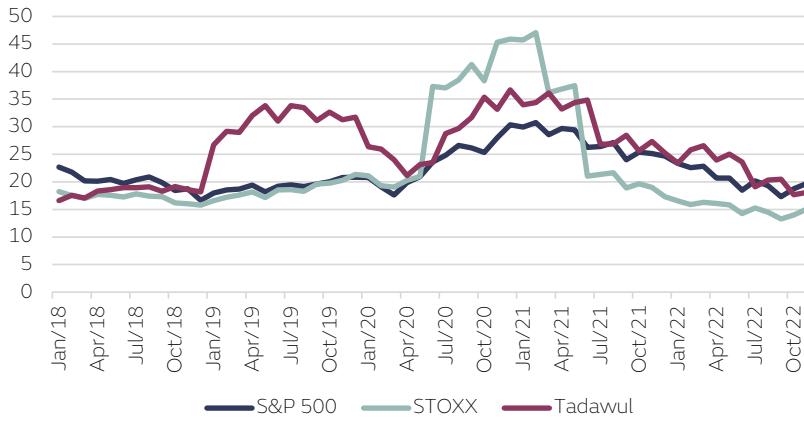
Policy responses to changing factors, particularly inflation, also create an altered operating environment. For example, Central Bank rate hikes drive up the cost of trade finance at the same time that global trading activity faces other input challenges. The fundamental price for discounting and acceptances (the bread and butter of trade finance) has increased over eight-fold since the pre-pandemic period.



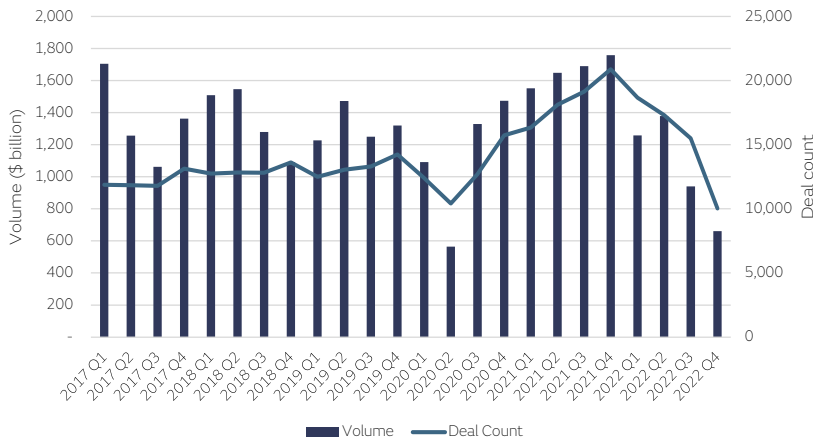
Source: Bloomberg

Accordingly we should not be surprised this holiday season that public equity prices and M&A activity (and prices) are fundamentally lower than the prior three year period.

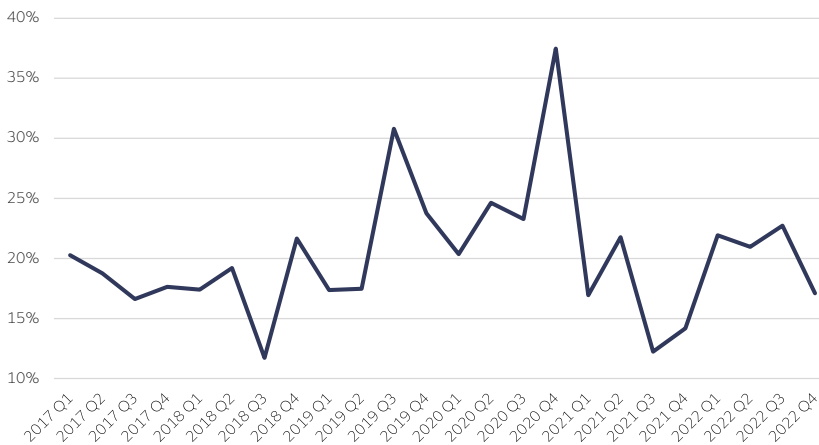
P/E Ratios



Global M&A



Average M&A Price Premium



Source: Bloomberg

In this environment we suggest investing based on specific factors driving 3-5 year returns rather than a forecast for 2023. Happy New Year everyone!

Feel free to contact us at info@gibam.com.

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