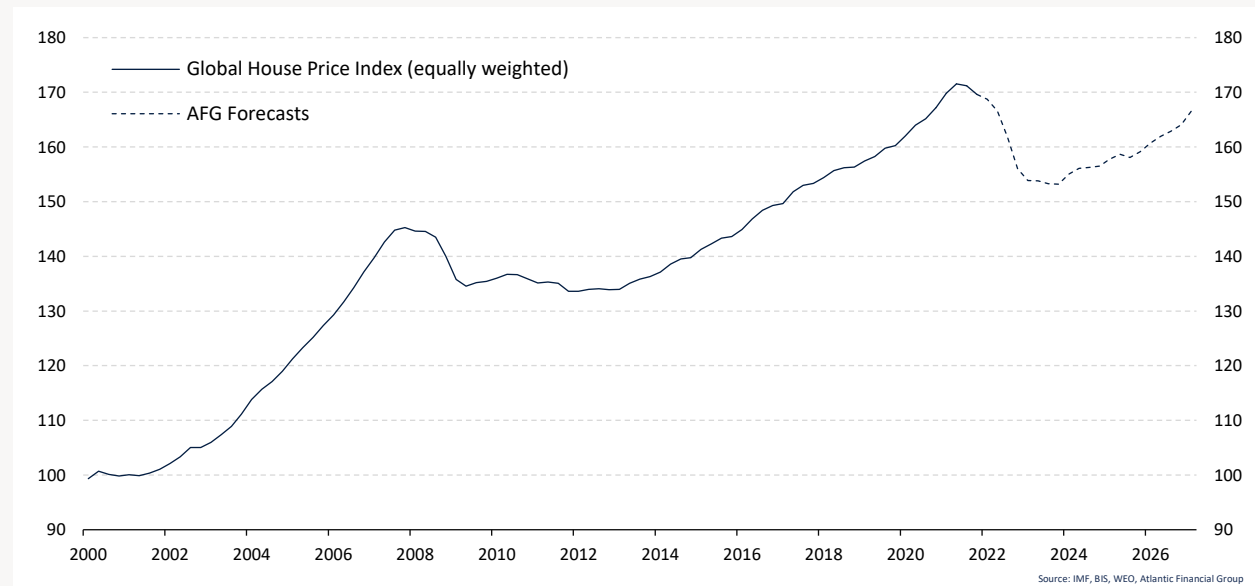




"END OF EUPHORIA IN THE HOUSING MARKET"

- ◆ The pandemic inflated the housing bubble, but two parameters have just changed:
- ◆ ... rising mortgage rates and tighter credit conditions
- ◆ During the crisis, investors will turn more to market experts
- ◆ ... in order to identify the best opportunities: life annuity, storage, agricultural land

CHART OF THE WEEK: "Evolution & forecast of the global housing market"

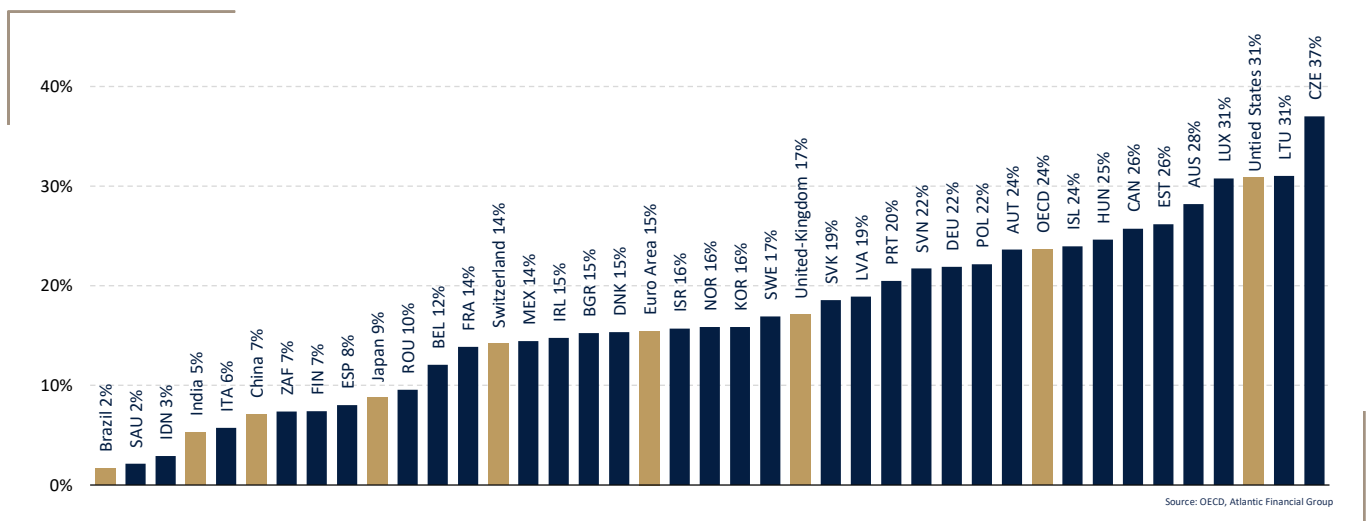


REAL ESTATE MARKET ANALYSIS

After the subprime crisis in 2008-09, the housing market began a period of healthy stabilisation in 2010-11, followed by a slow and steady price appreciation between 2012 and 2019. Global economic growth allowed housing construction to proceed at a moderate pace, while demand was underpinned not only by rising household wealth but also by their well-established expectations of long-term capital gains. In 2020 and 2021, under the influence of the health crisis, prices tended to rise more rapidly (see Fig. 2). Several factors explain this phenomenon.



Fig. 2 - Global housing market performance between 2019 and 2021



On the demand side:

- Lockdowns have increased the desire to live in spacious places
- Heavy fiscal packages have led to a surge in household savings
- The low interest rate environment has reduced mortgage funding costs
- The banks have applied particularly advantageous conditions for access to credit

On the supply side:

- The initial stock of goods for sale was relatively small
- Lockdowns have hampered the production of raw and construction materials
- Logistical problems have hampered the transport of these materials
- Soaring energy prices have increased production costs

All over the world, in an environment of strong demand and limited supply, property prices have soared to new heights (see Chart of the week). This overheating of the property market has led to major imbalances. There are many ratios that allow us to visualise this phenomenon. We will focus on just three of them here.

1. House prices in relation to household disposable income is without doubt the most important indicator. Households buy property mainly because they can afford it. The correlation between house price growth and disposable income growth is very strong. There is sometimes a lag of a few years between the two series, due to behavioural biases of households or public policies, but the link is strong. The ratio is now at record levels all over the world (see Fig. 3).
2. The housing affordability index (see Fig. 4) is widely used in the US. It measures whether the average family has a sufficiently high income to qualify for a mortgage to buy a standard home. While it is similar to the previous ratio, it introduces the concept of mortgage rate. The higher the rate, the lower the borrowing capacity of households. In concrete terms, a housing affordability index of 200 means



that the average household income is twice as high as the income needed to obtain a mortgage. Today, at 109, it is only 9% above the minimum income required.

Fig. 3 - House prices / household income

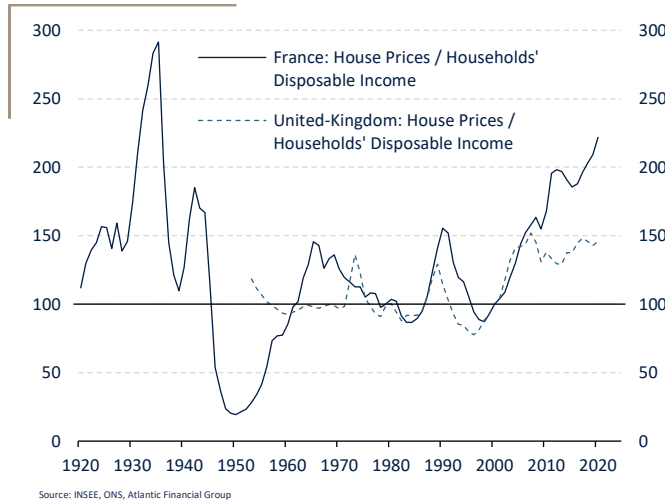
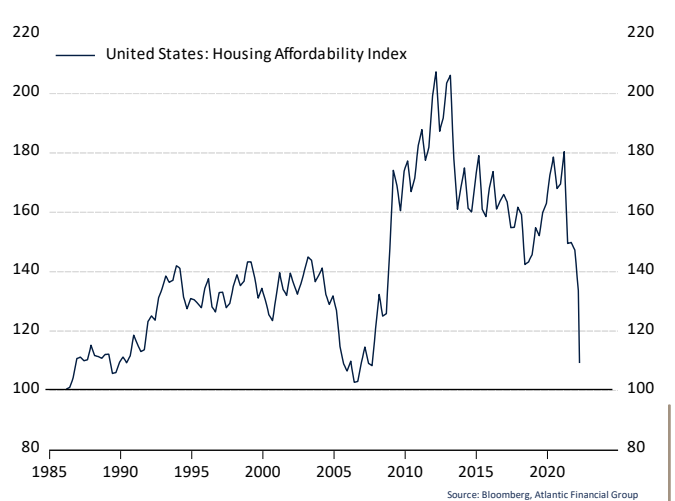
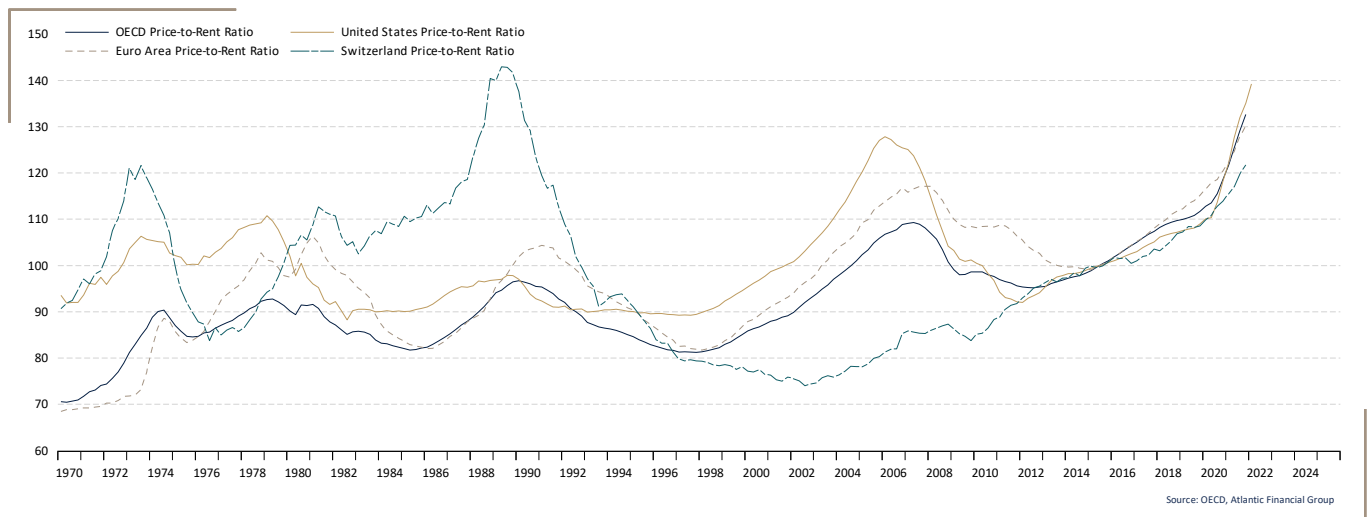


Fig. 4 - US housing affordability index



3. The price of housing in relation to rents gives investors a quick overview of rental profitability, but above all it reflects the trade-off that households make between buying and renting their homes (see Fig. 5). If the ratio is too high, as it is at present, then there are fewer buyers. As supply is relatively inelastic, demand will weaken until prices adjust downwards.

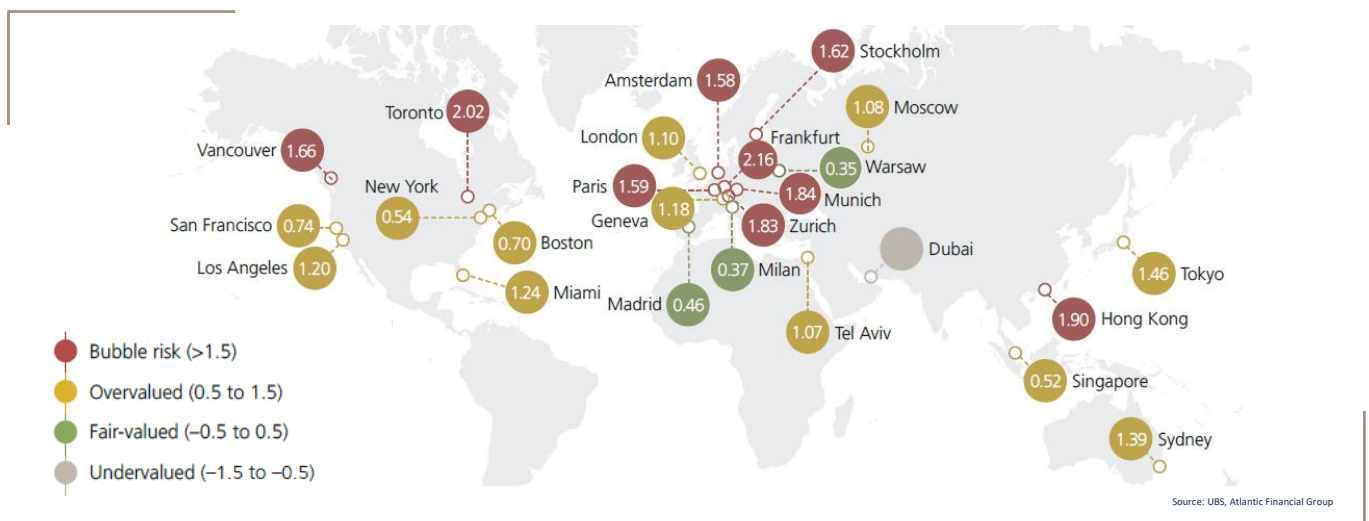
Fig. 5 - Property prices / annual rents



According to the UBS, the riskiest markets are Germany, Hong Kong, Canada, Switzerland, and also Sweden, the Netherlands and France (see Figure 6). According to the OECD, the most overvalued markets are New Zealand, Australia, and Canada.



Fig. 6 - UBS Housing Bubble Index



Just because a market is in a bubble does not mean that prices must necessarily and instantly fall to clear the situation. They can remain high for several years before normalising. Other variables can also adjust to make prices relatively fair. **Unfortunately, in the current case, two factors have recently come to darken the picture. They imply a high risk of contraction in 2022 and beyond:**

- **Inflation** is running at 8% per year, a situation not seen for 40 years. As prices are rising much faster than wages, it is eroding the purchasing power of households. Households have to choose between spending on basic goods (food, health, running costs) and discretionary goods (leisure, luxury goods, cars, as well as housing).
- **Commercial banks are increasing mortgage financing costs**, forced to pass on the rise in central bank interest rates, and the expected increase in their bad loans. **In addition, they are tightening lending conditions**, for example by requiring additional equity capital. More and more households are giving up on buying a house because they cannot get mortgage financing from a commercial bank. Banks believe that borrowers are not creditworthy enough, but they are also forced to drastically reduce their home loan lending in order to improve their own balance sheets. In countries subject to Basel III rules (where the strengthening of the level and quality of capital allows for increased liquidity risk management) the phenomenon is more visible. As an explicit example, in France, Société Générale and Crédit du Nord have suspended lending to brokers, who carry nearly 40% of the business, because the conditions have become too restrictive and the margins too low.

With supply constrained and prices high, a contraction in prices seems unavoidable in 2022 and beyond to reflect the slowdown in housing demand discussed above. The fall in prices has already begun in several major markets, notably in the main US and European cities. This correction could even be accentuated if the economic growth outlook were to deteriorate, for example with a recession, or if inflationary pressures were to persist, due to a deterioration in the geopolitical environment among other things. Finally, the tightening of monetary policy is likely to be much more damaging than expected. The



Australian central bank has estimated that a 2% increase in its key interest rate could lead to a 15% fall in house prices over a two-year period.

United States: In Uncle Sam's country, after soaring in 2020 and 2021 (cf. Fig. 7), home sales and prices are falling in some large cities, mainly because of rising mortgage rates (cf. Fig. 8). 6% of sellers have already conceded a fall in their sales price and this trend is expected to increase.

Fig. 7 - US housing market

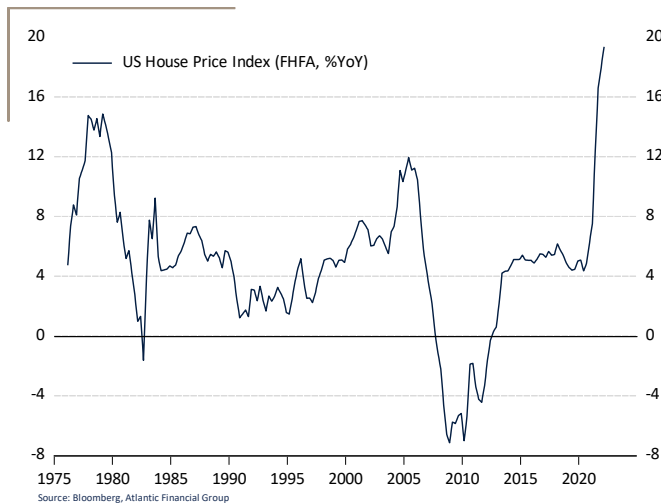
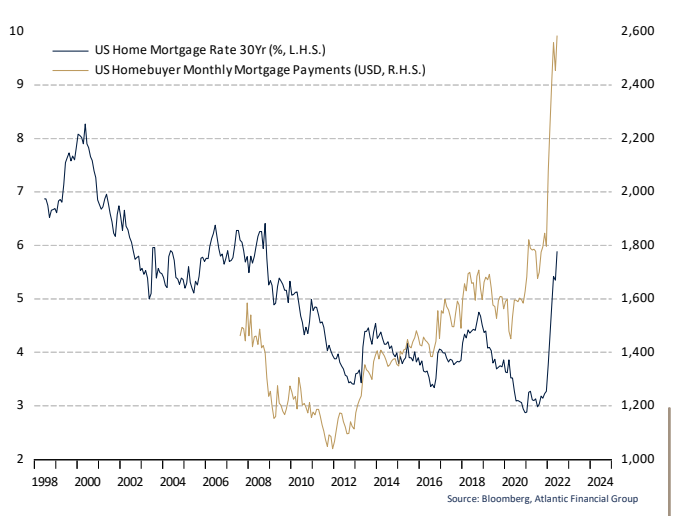


Fig. 8 - US mortgage rates and payments



China: Rules to curb excessive property price rises (the "three red lines" introduced in August 2020) have led to tighter liquidity conditions for property companies and to defaults, such as Evergrande, or downgrades, such as Greenland. Over the next few years, the continuation of this strategy will continue to put downward pressure on prices. In May 2022, for the first time since 2015, the price of new homes fell.

France: Residential property prices have continued to rise by more than 7% over the last twelve months. Houses in the provinces and single-family homes are still supporting the rise, while prices in Paris have been losing momentum since 2020. The next publications will be much less encouraging, as the rise in mortgage rates takes its toll.

Switzerland: Due to the strong real estate market, the Federal Council has decided to reactivate the anti-cyclical capital buffer from September 2022 and increase it to 2.5% of risk-weighted positions secured by real estate pledges on residential properties in Switzerland.



Among the sectors of the residential property market that should continue to benefit from their strong fundamentals are:

- **Luxury real estate, historic districts or "golden triangles":** In every market crisis, whether it is a bond, stock market or real estate crisis, the assets with the strongest fundamentals hold up better than those that have grown by mimicry but whose investment rationale is not robust. This tautology will direct real estate investors to properties in structurally attractive areas, where the size of the property matches the most sought-after demand and where the interior facilities and services offered on the outside are the most in demand. These properties are **often owned by the most affluent investors**, those with the experience and ability to weather crises without having to sell at any price to meet their day-to-day consumption and health needs. **Prices are therefore less volatile in the most sought-after neighbourhoods and at the very top end of the market than the market as a whole.** Buying during a crisis is a long-term bargain.
- **Life annuity:** A so-called "random" variant of real estate sales, **it consists of selling a property to a third party in exchange for a "bouquet"**, i.e. a sum of money paid in cash when the deed of sale is signed, followed by the payment of a periodic life annuity, often monthly, **until the unforeseeable death of the buyer.** It therefore allows people who own their own home, often elderly, to transform part of their capital into cash, without passing on their property to their heirs. The life annuity sale is based on the principle of uncertainty since, at the time of signing the deed of sale, neither the seller nor the buyer knows for what amount the property will be acquired. This amount will depend on the date of the seller's death.

Investors are understandably reluctant to speculate on the death of an elderly person. Fortunately, this is not the case. The life expectancy of the seller is in no way affected by the establishment of the life annuity. The life annuity is an exchange of good practices between an owner who wishes to sell his property and a provider of cash who wishes to invest. This transaction makes it possible to restore purchasing power to those who wish to do so, mainly retired people wishing to receive additional income and an annuity for the rest of their lives. In this way, life annuities can improve the living conditions of elderly people and, if they so wish, help them to remain in their own homes. **The purchasing power of the elderly is becoming a key issue as the world's population ages.** With the increase in the number of pensioners, longer life expectancy, and the decrease in the number of working people, **the balance of the pension system will become more and more uncertain.**

Moreover, the purchasing power of the elderly is not guaranteed. On the contrary, senior citizens are currently experiencing a punishing scissors effect: inflation of their expenses and low growth of their pensions. At a time in their lives when the need for assistance is increasing, this creates major financial imbalances. Life annuities are one of the few options for making a substantial part of their assets liquid and guaranteeing their living conditions. **In an environment of crisis in purchasing power, the life annuity market has a promising future,** particularly in countries such as France and Belgium where it is already established.



Beyond the residential sector, there are segments that attract our attention:

- **Warehouse real estate:** In recent years, online retailers such as Amazon have been particularly keen to **build warehouses to address their logistics and "last mile delivery" issues**. In the US, over eight million square metres of new warehouse space was delivered in the first quarter of 2022. Despite this, the rate of available space continues to fall and is now 3.4%. Demand is such that prices have tripled in six years. Private equity giants such as Blackstone, KKR, Carlyle, Apollo, and Sweden's EQT have all bought up sites to ride the warehousing wave. The tyranny of instant delivery is not over. The big brands are bound to multiply storage locations to get closer to their customers, especially in suburban areas. However, the hype has been such that a pause is likely.

Demand is expected to remain much more robust for data centres. Driven by e-commerce, 5G, streaming, but as well as the metaverse in the future, the segment is expected to continue to grow strongly. Between 2016 and 2021, the main European markets - London, Paris, Frankfurt, Amsterdam - doubled or tripled their digital storage capacity. The only question that remains is how many buildings to build, because for data centres, surface area is not sold in square metres but in megawatts of electrical capacity.

- **Agricultural land.** Often overlooked, this real asset has a strong potential for price growth. Investing in agricultural land means **owning arable land in order to rent it to a farmer who will farm the land** in return for a lease, i.e. a regular rent.

Like forests or vineyards, agricultural land benefits from the current economic and geopolitical context where agricultural commodity prices have risen sharply and even more so in a scenario where these prices are expected to remain structurally high.

Moreover, in an environment of rapid population growth, the need for food will increase. This phenomenon will be more noticeable as climate change, with its increasing number of natural disasters, will certainly prevent food supply from keeping pace with demand. The price of farmland is therefore likely to rise sharply.

Projects that base their strategy on sustainable, socially responsible agriculture, **and also aim to relocate the production of plant species in Europe**, will benefit from the current enthusiasm of consumers, industry, investors, and governments.

Conclusion:

The global housing market has been steadily growing since 2012. This trend accelerated during the Covid-19 pandemic, pushing house prices to new heights. In the current economic and financial conditions, a deflation of the housing bubble seems inevitable. More than ever, investors will be looking for guidance from industry experts. In any crisis, there are opportunities. It is still necessary to be able to detect them, finance them, promote them, and manage them in order to grab them: life annuity, storage property and agricultural land.





RETURN ON FINANCIAL ASSETS

Markets Performances (local currencies)	Last Price	Momentum Indicator (RSI)	1-Week (%)	1-Month (%)	2022 Year-to-Date (%)	2021 (%)	2020 (%)
Equities							
World (MSCI)	584.6	29.07	-5.7%	-8.5%	-21.7%	19.0%	16.9%
USA (S&P 500)	3 675	31.77	-5.7%	-10.0%	-22.3%	28.7%	18.4%
USA (Dow Jones)	29 889	30.11	-4.7%	-8.2%	-16.9%	20.9%	9.7%
USA (Nasdaq)	10 798	36.85	-4.8%	-9.8%	-30.7%	22.2%	45.0%
Euro Area (DJ EuroStoxx)	384.2	33.07	-4.6%	-7.6%	-17.7%	23.5%	0.8%
UK (FTSE 100)	7 016	31.20	-4.1%	-6.3%	-3.2%	18.4%	-11.4%
Switzerland (SMI)	10 451	21.96	-5.7%	-10.8%	-16.6%	23.7%	4.3%
Japan (Nikkei)	25 679	35.81	-6.7%	-2.6%	-8.9%	6.7%	18.3%
Emerging (MSCI)	1 005	36.61	-4.7%	-2.1%	-17.5%	-2.3%	18.8%
Brasil (IBOVESPA)	99 825	25.64	-5.4%	-8.2%	-4.8%	-11.9%	2.9%
Russia (MOEX)	2 354	49.27	3.0%	-2.3%	-37.0%	21.9%	14.8%
India (SENSEX)	51 423	29.15	-5.3%	-5.0%	-11.1%	23.2%	17.2%
China (CSI)	4 349	65.56	1.8%	8.1%	-12.2%	-3.5%	29.9%
Communication Serv. (MSCI World)	79.43	35.48	-4.9%	-8.0%	-27.6%	10.9%	24.2%
Consumer Discret. (MSCI World)	283.2	36.83	-5.4%	-6.9%	-30.5%	9.2%	37.0%
Consumer Staples (MSCI World)	248.7	25.67	-3.5%	-8.7%	-13.7%	11.7%	8.8%
Energy (MSCI World)	213.7	27.13	-14.4%	-10.4%	15.8%	37.5%	-27.7%
Financials (MSCI World)	123.0	28.19	-4.4%	-7.3%	-16.8%	25.1%	-3.1%
Health Care (MSCI World)	306.9	27.67	-4.4%	-7.8%	-16.1%	18.0%	15.4%
Industrials (MSCI World)	255.4	26.94	-6.0%	-8.6%	-22.2%	16.6%	11.8%
Info. Tech. (MSCI World)	396.6	33.56	-5.5%	-9.9%	-30.6%	27.6%	46.2%
Materials (MSCI World)	305.7	25.09	-7.9%	-8.8%	-14.6%	15.4%	21.6%
Real Estate (MSCI World)	181.2	26.82	-5.1%	-8.5%	-21.8%	23.6%	-5.7%
Utilities (MSCI World)	143.5	21.74	-7.6%	-9.4%	-10.4%	11.1%	4.8%
Bonds (FTSE)							
USA (7-10 Yr)	3.23%	41.19	-0.5%	-1.6%	-11.8%	-2.4%	9.3%
Euro Area (7-10 Yr)	2.36%	33.63	-0.5%	-4.9%	-14.5%	-2.9%	4.5%
Germany (7-10 Yr)	1.66%	24.18	-1.5%	-5.1%	-13.2%	-2.7%	3.0%
UK (7-10 Yr)	2.50%	31.68	-0.5%	-4.5%	-10.3%	-4.9%	5.4%
Switzerland (7-10 Yr)	1.39%	25.31	-2.3%	-5.1%	-12.1%	-2.3%	0.4%
Japan (5-10 Yr)	0.24%	41.03	-0.3%	-0.3%	-1.5%	0.0%	-0.1%
Emerging (5-10 Yr)	7.76%	26.60	0.0%	-3.3%	-19.4%	-2.3%	5.2%
USA (IG Corp.)	4.79%	37.00	0.8%	-2.2%	-14.9%	-1.0%	9.9%
Euro Area (IG Corp.)	3.38%	18.01	-0.8%	-4.8%	-12.6%	-1.0%	2.8%
Emerging (IG Corp.)	7.45%	24.92	-0.6%	-2.0%	-15.5%	-3.0%	8.1%
USA (HY Corp.)	8.51%	27.49	-0.3%	-2.3%	-13.1%	5.3%	7.1%
Euro Area (HY Corp.)	7.14%	13.42	-1.6%	-4.0%	-12.3%	3.4%	2.3%
Emerging (HY Corp.)	10.90%	22.97	-0.6%	-3.5%	-16.0%	-3.2%	4.3%
World (Convertibles)	348.1	28.19	-4.6%	-5.3%	-20.6%	2.4%	38.8%
USA (Convertibles)	459.7	30.64	-5.2%	-5.8%	-22.5%	3.1%	54.5%
Euro Area (Convertibles)	3 416	17.44	-3.7%	-5.5%	-16.8%	-0.3%	6.1%
Switzerland (Convertibles)	171.2	21.42	-1.5%	-3.7%	-7.9%	-0.5%	0.5%
Japan (Convertibles)	194.3	33.66	-1.7%	-0.8%	-3.2%	3.3%	2.8%
Hedge Funds (Crédit Suisse)							
Hedge Funds Indus.	745.03	72.28	n.a.	-0.6%	n.a.	8.2%	6.4%
Distressed	965.81	66.22	n.a.	-1.3%	n.a.	12.5%	3.8%
Event Driven	788.05	58.63	n.a.	-1.3%	n.a.	12.9%	7.0%
Fixed Income	387.63	67.19	n.a.	0.3%	n.a.	5.2%	3.6%
Global Macro	1443.12	85.56	n.a.	1.6%	n.a.	9.6%	6.5%
Long/Short	879.97	53.98	n.a.	-0.5%	n.a.	8.3%	7.9%
CTA's	400.78	79.04	n.a.	-0.1%	n.a.	8.2%	1.9%
Market Neutral	287.22	62.27	n.a.	1.2%	n.a.	6.2%	1.7%
Multi-Strategy	727.66	62.30	n.a.	-3.9%	n.a.	7.0%	5.6%
Volatility							
VIX	31.13	55.55	12.2%	19.3%	80.8%	-24.3%	65.1%
VSTOXX	30.89	56.92	11.7%	17.7%	60.3%	-17.6%	67.5%
Commodities							
Commodities (CRB)	617.5	n.a.	-1.9%	-3.1%	6.8%	30.3%	10.5%
Gold (Troy Ounce)	1 842	47.82	1.3%	-0.2%	0.7%	-3.6%	25.1%
Oil (WTI, Barrel)	109.56	41.39	-9.4%	-2.5%	42.3%	58.7%	-20.5%
Oil (Brent, Barrel)	117.38	46.05	-7.0%	2.6%	51.1%	51.4%	-23.0%
Currencies (vs USD)							
USD (Dollar Index)	104.39	57.49	-0.7%	1.2%	9.1%	6.4%	-6.7%
EUR	1.0527	45.12	1.1%	-0.4%	-7.4%	-7.5%	9.7%
JPY	135.00	34.23	-0.4%	-5.3%	-14.8%	-10.2%	5.1%
GBP	1.2239	42.55	0.9%	-1.9%	-9.6%	-1.0%	3.1%
AUD	0.6965	42.79	0.6%	-1.1%	-4.1%	-5.6%	9.6%
CAD	1.3003	36.43	-0.8%	-1.3%	-2.8%	0.7%	2.1%
CHF	0.9657	55.32	3.3%	0.9%	-5.5%	-3.0%	9.4%
CNY	6.6822	49.19	1.1%	0.2%	-4.9%	2.7%	6.7%
MXN	20.299	41.66	0.8%	-2.1%	1.1%	-3.0%	-5.0%
EM (Emerging Index)	1 672.6	35.57	-0.6%	-0.2%	-3.6%	0.9%	3.3%

Source: Bloomberg, Atlantic Financial Group

Total Return by asset class (Negative \ Positive Performance)



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