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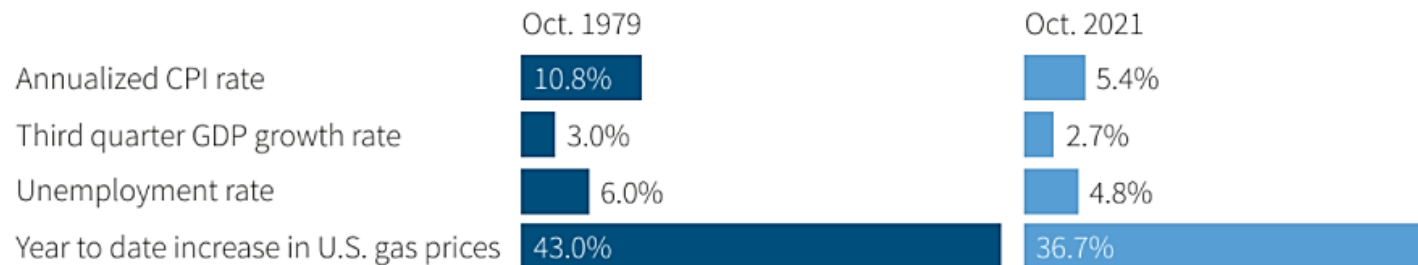
## ONE Insight

What to invest under hyper inflation?

# Price keeps rising, Fed is trying to prevent what happened in the 1970s

There's a rising concern that the US economy will fall back into a period of stalling growth and high inflation similar to the late 1970s. The late 1970s stagflation era ended when the federal Reserve began raising interest in December 1979, eventually reaching a record 20% the following year. The latest November Fed meeting summary noted that the officials would be willing to raise interest rates "sooner than participants currently anticipated."

● Oct. 1979 ● Oct. 2021



Note: Estimated Q3 GDP growth rate

Sources: The Federal Reserve, U.S. Energy Information Administration, Bureau of Labor Statistics

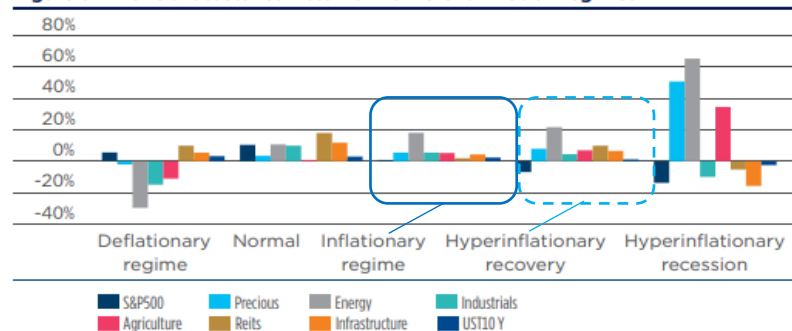
# Learning from history: What to invest under (hyper) inflation?

Here's an analysis of the S&P historical performance by sector from 1960 to 2018 under different inflation policies enacted by Fed.

| Regimes                     | CPI YoY (%) | PPI YoY (%) | PCE YoY (%) | Unit labour cost YoY (%) |
|-----------------------------|-------------|-------------|-------------|--------------------------|
| Deflationary regime         | <2          | <1          | <2          | <1                       |
| Normal                      | 2-3         | 2-3         | 2-3         | 2-3                      |
| Inflationary regime         | 3-6         | 3-6         | 3-6         | 3-6                      |
| Hyperinflationary recovery  | 6-10        | 6-10        | 6-8         | 6-9                      |
| Hyperinflationary recession | >10         | >10         | >8          | >9                       |

When under an inflationary regime (similar to now), or even hyperinflationary regime (might happen soon), sectors that out performed others are mainly Energy, REITs and commodities like precious metals.

**Figure 8: Financial assets real returns in different inflation regimes**



Source: Amundi Research. Data as of 24 April 2019. S&P500, US global REITS from global financial data; US 10Yrs from Bloomberg; global infrastructure (equities), total returns series proxied by a basket of 50% utilities and 50% transportation; precious metal: GSCI Precious Metals Total Return Index, proxied by gold before index starts; Energy: GSCI Energy Total Return Index, proxied by Brent Crude Oil before index starts; Industrial metals: GSCI Industrial Metals Total Return Index, proxied by copper before index starts; Agriculture: GSCI Agriculture Total Return Index.

<sup>1</sup>To feed cluster analysis, regimes are identified by US CPI yoy change, US PPI yoy change, US PCE Core yoy change and US ULC.

# Learning from history: What to invest under (hyper) inflation?

When breaking down into years

  = inflation > 3%

Oil shortage

The dotcom bubble

Financial crisis

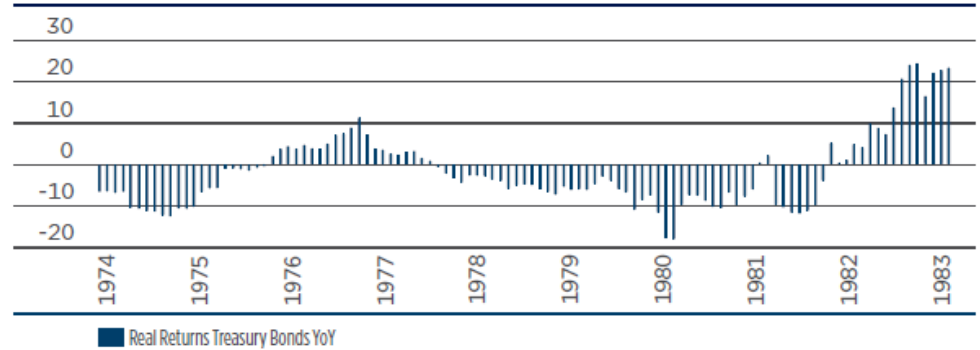
| Year | Reference |                | Annual Nominal Return |                  |             |           |             |             |         |                        |           |            |                        |                  |  |
|------|-----------|----------------|-----------------------|------------------|-------------|-----------|-------------|-------------|---------|------------------------|-----------|------------|------------------------|------------------|--|
|      | Inflation | Treasury Bills | S&P 500               | Consumer Staples | Health Care | Utilities | Real Estate | Industrials | Energy  | Consumer Discretionary | Materials | Financials | Information Technology | Telecom Services |  |
| 1976 | 4.86      | 5.01           | 23.70                 | 12.70            | 1.80        | 34.00     | 47.22       | 32.70       | 34.90   | 17.80                  | 22.90     | 34.70      | 25.20                  | 34.90            |  |
| 1977 | 6.70      | 5.01           | (7.95)                | (4.65)           | (9.65)      | 9.45      | 22.08       | (4.15)      | (2.65)  | (15.65)                | (23.65)   | (11.45)    | (5.45)                 | 1.65             |  |
| 1978 | 9.02      | 7.10           | 5.90                  | 4.80             | 8.50        | (6.00)    | 10.01       | 9.20        | 11.10   | (0.30)                 | 0.60      | 5.10       | 13.80                  | 5.40             |  |
| 1979 | 13.23     | 10.30          | 18.00                 | 4.00             | 23.00       | 14.10     | 35.55       | 20.00       | 44.90   | 8.70                   | 32.00     | 17.90      | 5.00                   | (0.90)           |  |
| 1980 | 12.52     | 11.20          | 31.90                 | 14.80            | 30.70       | 16.40     | 24.08       | 39.70       | 73.90   | 17.50                  | 27.30     | 16.90      | 16.80                  | 2.90             |  |
| 1981 | 8.92      | 14.60          | (5.20)                | 17.20            | 3.10        | 8.60      | 5.73        | (12.50)     | (23.90) | 5.80                   | (9.00)    | 10.20      | (15.70)                | 34.40            |  |
| 1982 | 3.83      | 10.40          | 20.90                 | 36.90            | 21.30       | 28.40     | 21.28       | 21.70       | (12.90) | 47.90                  | 8.90      | 23.90      | 53.50                  | 13.50            |  |
| 1983 | 3.79      | 8.70           | 21.30                 | 17.70            | 6.40        | 18.30     | 30.26       | 31.70       | 24.60   | 20.80                  | 27.90     | 17.20      | 26.20                  | 10.50            |  |
| 1984 | 3.95      | 9.70           | 6.21                  | 14.71            | 6.41        | 26.71     | 20.59       | (0.79)      | 8.01    | 3.71                   | (7.09)    | 10.61      | (0.99)                 | 20.51            |  |
| 1985 | 3.80      | 7.37           | 31.23                 | 42.93            | 42.43       | 27.63     | 18.79       | 29.53       | 18.03   | 31.53                  | 30.33     | 40.43      | 23.23                  | 38.23            |  |
| 1986 | 1.10      | 6.00           | 18.06                 | 33.16            | 29.66       | 25.56     | 18.89       | 16.66       | 16.36   | 19.86                  | 25.56     | 10.16      | (6.94)                 | 23.76            |  |
| 1987 | 4.43      | 6.12           | 4.71                  | 11.51            | 6.11        | (7.89)    | (3.85)      | 2.11        | 8.21    | 0.91                   | 21.81     | (17.19)    | 13.61                  | 4.61             |  |
| 1988 | 4.42      | 7.18           | 16.22                 | 19.42            | 12.62       | 14.72     | 13.21       | 12.02       | 21.02   | 24.42                  | 9.82      | 16.92      | (2.78)                 | 20.92            |  |
| 1989 | 4.65      | 8.87           | 31.36                 | 47.96            | 42.56       | 37.56     | 8.52        | 26.56       | 40.05   | 21.06                  | 22.16     | 33.06      | (6.24)                 | 61.26            |  |
| 1990 | 6.11      | 7.94           | (3.32)                | 17.58            | 13.98       | (0.72)    | (15.62)     | (6.72)      | 3.38    | (14.22)                | (11.82)   | (21.62)    | 2.08                   | (15.42)          |  |
| 1991 | 3.06      | 5.73           | 30.22                 | 48.02            | 51.82       | 23.72     | 35.35       | 29.22       | 55.42   | 28.62                  | 24.72     | 49.62      | 12.22                  | 13.82            |  |
| 1992 | 2.90      | 3.53           | 7.42                  | 6.62             | (15.78)     | 8.32      | 14.30       | 9.42        | 12.72   | 19.52                  | 10.32     | 23.22      | 3.22                   | 16.22            |  |
| 1993 | 2.75      | 2.86           | 9.89                  | (6.81)           | (6.01)      | 13.39     | 19.39       | 19.49       | 12.59   | 20.49                  | 14.39     | 10.99      | 19.59                  | 14.79            |  |
| 1994 | 2.67      | 3.81           | 1.18                  | 5.68             | 13.18       | (11.62)   | 2.93        | (2.92)      | 2.48    | (7.22)                 | 5.18      | (3.42)     | 19.68                  | (4.62)           |  |
| 1995 | 2.54      | 5.49           | 37.45                 | 36.75            | 58.45       | 31.35     | 15.00       | 39.65       | 30.25   | 22.05                  | 17.35     | 53.65      | 38.45                  | 41.05            |  |
| 1996 | 3.32      | 5.09           | 22.88                 | 24.48            | 22.08       | 4.08      | 34.95       | 24.78       | 25.58   | 13.78                  | 13.38     | 36.18      | 42.18                  | 0.68             |  |
| 1997 | 1.70      | 5.12           | 33.19                 | 36.69            | 41.09       | 24.79     | 18.46       | 27.49       | 24.59   | 29.39                  | 7.79      | 49.39      | 27.89                  | 40.49            |  |
| 1998 | 1.61      | 5.00           | 28.62                 | 22.92            | 41.42       | 14.42     | (16.32)     | 9.52        | 2.52    | 33.12                  | (8.48)    | 9.12       | 77.12                  | 51.62            |  |
| 1999 | 2.68      | 4.55           | 21.07                 | (1.63)           | (9.33)      | (9.73)    | (4.04)      | 19.07       | 15.07   | 20.97                  | 30.07     | 3.77       | 77.47                  | 19.67            |  |
| 2000 | 3.39      | 5.80           | (9.06)                | 5.64             | 38.24       | 58.44     | 26.35       | 3.94        | 20.04   | (24.26)                | (17.86)   | 25.94      | (38.46)                | (37.96)          |  |
| 2001 | 1.55      | 3.99           | (12.02)               | (3.32)           | (12.22)     | (32.22)   | 12.35       | (7.52)      | (11.02) | 4.48                   | 3.28      | (9.02)     | (25.02)                | (12.42)          |  |
| 2002 | 2.38      | 1.51           | (22.15)               | (6.65)           | (19.25)     | (21.45)   | 3.75        | (25.85)     | (16.25) | (26.05)                | (7.55)    | (14.15)    | (36.85)                | (33.85)          |  |
| 2003 | 1.88      | 0.82           | 28.50                 | 15.70            | 14.90       | 24.00     | 35.65       | 32.20       | 26.00   | 35.30                  | 38.20     | 32.00      | 46.70                  | 6.80             |  |
| 2004 | 3.26      | 1.00           | 10.74                 | 8.24             | 1.84        | 20.24     | 30.76       | 18.64       | 31.14   | 10.94                  | 13.54     | 10.24      | 4.44                   | 19.14            |  |
| 2005 | 3.42      | 2.77           | 4.77                  | 3.37             | 5.87        | 14.47     | 11.89       | 1.87        | 31.27   | (5.23)                 | 4.57      | 6.27       | (0.33)                 | (4.53)           |  |
| 2006 | 2.54      | 4.55           | 15.64                 | 13.44            | 7.54        | 21.74     | 35.07       | 13.34       | 24.14   | 18.44                  | 18.64     | 19.64      | 7.94                   | 36.94            |  |
| 2007 | 4.08      | 4.65           | 5.39                  | 13.09            | 7.09        | 17.89     | (16.46)     | 11.69       | 34.29   | (13.01)                | 21.79     | (18.71)    | 16.89                  | 11.39            |  |
| 2008 | 0.09      | 1.97           | (37.02)               | (14.02)          | (23.42)     | (29.72)   | (37.05)     | (39.92)     | (35.62) | (34.12)                | (45.62)   | (55.32)    | (43.72)                | (31.02)          |  |
| 2009 | 2.72      | 0.53           | 26.49                 | 13.79            | 19.19       | 11.59     | 29.58       | 21.29       | 14.09   | 42.39                  | 48.39     | 16.09      | 62.09                  | 8.39             |  |
| 2010 | 1.50      | 0.01           | 14.91                 | 14.11            | 2.61        | 5.41      | 28.30       | 26.41       | 20.31   | 27.71                  | 22.11     | 12.11      | 10.01                  | 18.91            |  |
| 2011 | 2.96      | 0.02           | 1.97                  | 13.87            | 12.57       | 19.87     | 8.47        | (0.73)      | 4.57    | 5.97                   | (9.93)    | (17.23)    | 2.27                   | 6.17             |  |
| 2012 | 1.74      | 0.02           | 15.82                 | 10.62            | 17.72       | 1.12      | 17.53       | 15.12       | 4.42    | 23.72                  | 14.82     | 28.62      | 14.62                  | 18.12            |  |
| 2013 | 1.50      | 0.01           | 32.18                 | 26.27            | 41.24       | 13.00     | 2.31        | 40.44       | 26.16   | 42.72                  | 25.83     | 35.37      | 25.97                  | 24.32            |  |
| 2014 | 0.76      | 0.01           | 13.51                 | 15.86            | 25.18       | 28.59     | 30.13       | 10.45       | (8.60)  | 9.49                   | 7.31      | 15.03      | 17.75                  | 3.98             |  |
| 2015 | 0.73      | 0.02           | 1.25                  | 6.83             | 6.86        | (4.86)    | 2.22        | (4.25)      | (21.46) | 9.94                   | (8.58)    | (1.60)     | 5.63                   | 2.72             |  |

# Learning from history: Bond & its correlation with Equity

Bonds, which often considered as a complements to diversify risk from other assets, were valuable too under hyper inflation. Government bonds even had negative performances in real terms in the period from 1977 to 1980 as interest rates skyrocketed from 7.4% to almost 16% in 1981.

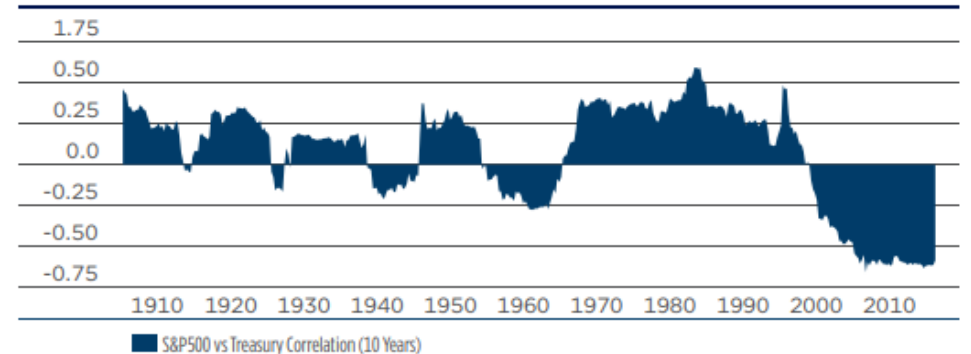
Equities and bonds can be treated as “complements” under a non-hyper-inflation condition.

**Bond Investors and the terrible 70s (US Treasury real returns, YoY, (%))**



Source: Bloomberg, data as at 3 April 2019. Rolling one-year real returns calculated on the Bloomberg Barclays US Treasury Index excess return vs. CPI YoY growth.

**Bond and equity correlation**



Source: Amundi elaboration on Global Financial Data. 10 years rolling correlation on quarterly data. Data as at end of 2018.

# Our takeaways

- Despite few short term fluctuations, **S&P** (S&P 500 YTD 25.17%) in general performed well during most inflation, and hyperinflation period in history. Investors should keep invested in stock markets.
- Among all the sectors in S&P, **Energy sector** out performed others the most during inflationary periods. There are Energy related ETFs, despite the challenging market environment, largely outperformed the market this year. E.g., the Energy Select Sector SPDR Fund (XLE, YTD 57.85%).
- **REITs**, another star player in the league. E.g. 823 HK Equity (Link REIT , YTD -1.7%,dividend yield 4.44% ); USRT US Equity (iShares Core US REIT, YTD 37.3%); REET US Equity (iShares Global REIT, YTD 27.3%)

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