



The Tireless Pursuit for Growth & Forging Partnerships through Innovative Solutions

Dear Friends,

2018 has been a remarkable year for Lighthouse Canton – with many milestones achieved from different aspects of the business. We started the year with a view to consolidate some of the initiatives we took in 2017 and we are pleased with the considerable progress we have made in terms of strengthening our infrastructure and teams in order for us to provide best-in-class services and solutions to our ever-growing investor base. Before another year wraps up and a new year kicks in, we would like to share the updates on our journey this year, what is in store next year as well as our view and outlook on the markets in terms of the challenges and opportunities it brings and how we look to navigate it.

Markets are entering the new year facing several challenges - maturing economic cycle, end of central bank support to markets, rising geopolitical risks, continued weakness in financial sector in major economies, high debt levels and rising volatility across asset classes. The fact that this has already been one of the longest bull markets in history does not add to confidence and it only increases the probability of further corrections in equities or even a full-blown bear market. As Governments have exhausted a lot of their fiscal and political capital already, the ammunition they have to bail out economies and markets in case of a severe downturn or crisis appears limited.

Therefore, while corporate earnings are robust and unemployment rate is low in the US, rate cycle is closer to a pause or have peaked, and valuations have fallen in the recent pull back, so it is important focus on risk mitigation even as one stays invested. It is critical to clearly map your risk appetite and define your strategy to deal with downside risks. Therefore, it is important to think in terms of strategy allocation, not just asset allocation.

Strategy allocation is not a term that we hear that often even among investment professionals. There are numerous articles on asset allocation and it is much easier to talk about asset allocation and sound like an expert, since everyone is doing it. Asset allocation often refers to long-only allocation to various asset classes to capitalise on market returns (beta) over the long term, whilst achieving diversification. However, chasing beta can be dangerous when markets are poised to roll over. Those who remember even just the previous two equity bear markets will recollect that equity markets can fall by over 50% and wipe out the capital of many investors, particularly those with leverage.

Strategy allocation on the other hand, requires an investigation into the game-plan that the portfolio manager has formulated (or not) for dealing with various market scenarios. These would include strategy for generating alpha, formula around entry and position sizing to increase probability of winning in the long-term without losing capital, diversification strategy, portfolio hedges and risk management rules.

We believe it is important to increase allocation to managers or strategies which are likely to earn decent returns if bull markets continue, but also have a clearly articulated and credible strategy to protect capital and profit from corrections and bear markets. Picking the right strategies has always been a focus for us



and hence we like managers and strategies that have a clearly defined game plan for dealing with adverse market conditions. As we enter the new year, we would look to increase allocation to market neutral, arbitrage and alternate income strategies that have low correlation to broader markets. We would aim to stay liquid and be wary of tying up too much of the portfolio into private investments or funds that require long lock-ups. We would avoid exposure to high yield, where the risk-reward appears unfavourable, unless it is through a strategy where risks are being hedged actively. We would continue to allocate a portion of the portfolio to long term growth equities, particularly in emerging markets, where valuations have corrected to reasonable levels in some high-quality businesses.

While we are cognisant of the market challenges which lies ahead, we also look forward to the opportunities this brings as we believe that we have the right strategy and people on-board. On behalf of the Lighthouse Canton team, we would like to sincerely thank you for your support and confidence in us and we look forward to growing in strength with you. We wish you Happy Holidays and may 2019 bring much success, happiness, wealth and joy to you and your loved ones.

Yours Faithfully,

Rajesh Sundaresan

CIO, Lighthouse Canton