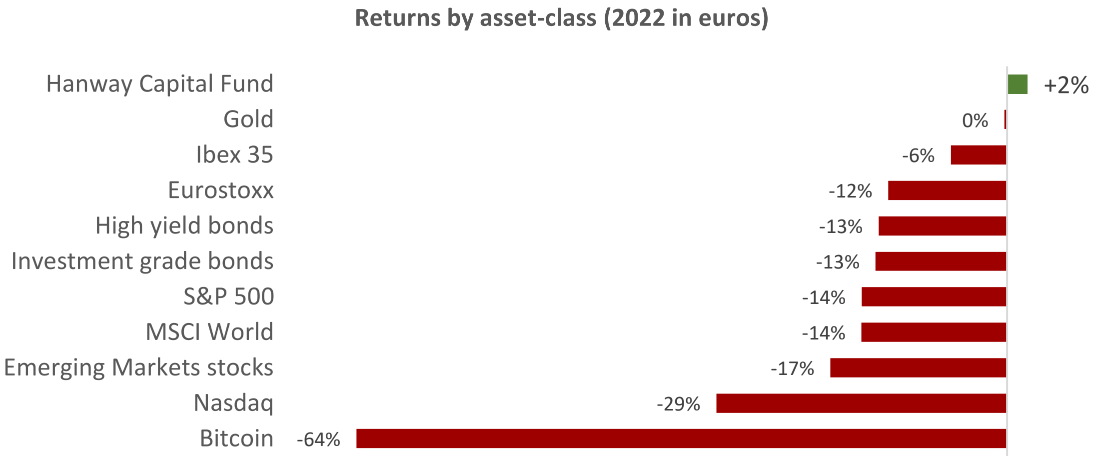
January 17th, 2022

Q4 2022

Dear Investors,

Hanway Capital Fund has returned **-2,0% this quarter** reaching a share price of **€148.6** net of fees and commissions. This brings the fund's **full year return to +2.0%**. In a generally challenging year, this has been a particularly difficult quarter to navigate: our overly defensive positioning has taken its toll. Although we have not generated an impressive return this year, we are pleased to have safeguarded our investors' capital when most alternatives have suffered major setbacks.



The year when tulips wilted

2022 will become part of the distinguished list of years in which stubborn reality prevails over excessive optimism and speculative bubbles come to an end. While progress is cumulative in science, it is definitively cyclical in finance; knowledge is often forgotten over time. Although we lived through a huge technology bubble just over 20 years ago, we have seen history repeat itself as a result of excess liquidity created to deal with the pandemic.

But financial bubbles are not exclusive to the 21st century: as long as the price of an asset is decided by the collective consensus of many human beings with herd behavior, we will continue to fill pages about the shortcomings of the efficient market theory.

At the beginning of the 17th Century, the United Provinces of the Netherlands had recently gained their independence from Habsburg Spain and were beginning to walk the path of a new republic that would quickly become the world's leading power of the time. The Dutch Golden Age began, where trade, science and culture flourished. Cradle of modern capitalism, the Dutch East India Company and the Bank of Amsterdam, considered by some as the first central bank, were founded.

The strong progress quickly enriched Dutch society and a new bourgeois class of merchants appeared. With their pockets full and their needs met, art and culture became fashionable collectibles. Thus it was that the Dutch became fascinated by the beauty of tulips, an exotic flower that came from the Ottoman Empire.

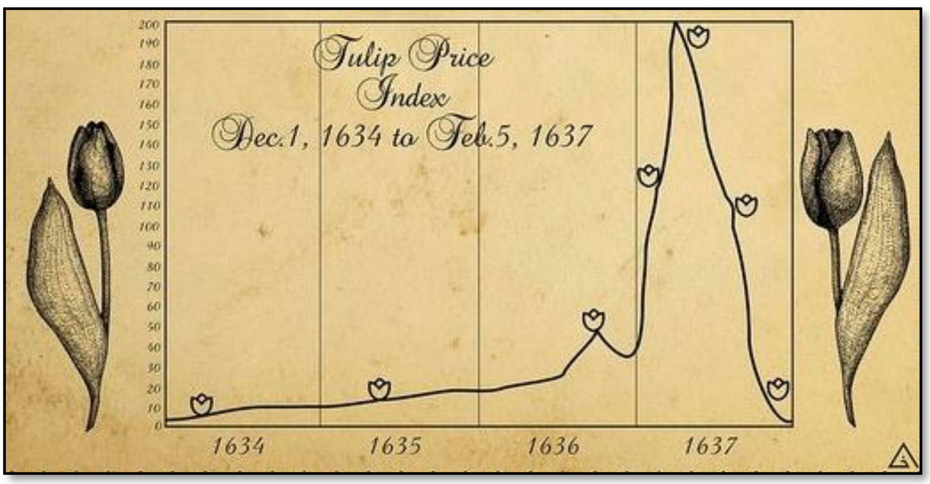
Carolus Clusius, a leading botanist working in the Imperial Gardens in Vienna, is credited with introducing the tulip to the Netherlands. He brought with him a collection of bulbs that generated a great result due to the fertility of the sandy soil reclaimed from the sea. Quickly the interest in flaunting this exotic flower as a symbol of wealth spread among the wealthy classes.

Everyone wanted tulips at home and the more exotic the better. The multicolored effects of intricate lines on the petals were vivid and spectacular, which made the bulbs that produced these even more bizarre looking plants highly sought. The rarest varieties were even named after illustrious characters.

As inventors of the first stock exchange market and fathers of modern finance, the Dutch were quick to create a market for tulip bulbs, with a futures market in which the buyer was assured of receiving the bulbs in time for them to bloom in April. Speculation soon began, tulip futures contracts changed hands multiple times without even exchanging bulbs.

In the 1620s, tulip prices began to rise rapidly. Everyone wanted to participate in the speculation, as there is nothing more unbearable than to hear acquaintances bragging about their financial gains if one does not share their luck. In 1634 the final phase of the mania began: luxurious mansions exchanged for a single bulb or flowers sold in exchange for six years' wages.

"What do you mean you haven't invested in tulips; don't you know that everyone is making a lot of money on them?" - these kinds of conversations became common in the Amsterdam of 1636. Who would want to miss out? The Dutch also started borrowing money to keep buying bulbs, speculating beyond their means. The price continued to escalate. Some probably began to wonder what purpose tulips would have, but even the most rational minds succumbed to the fear of missing out.

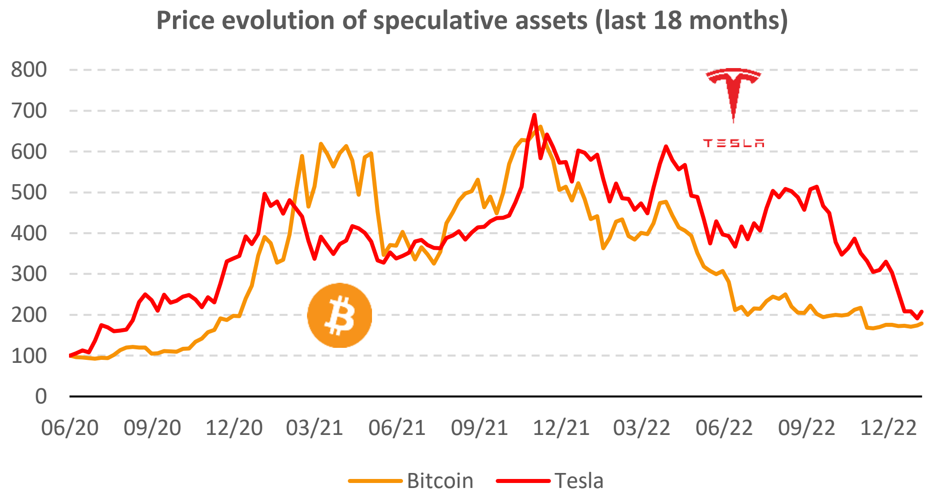


Although euphoria spread quickly, confidence faded even faster. On February 3rd, 1637, a lot of tulips was put up for sale without finding a buyer. The price of tulips began to fall as fast as their petals withered. Many investors went bankrupt due to debts incurred, which further precipitated the price decline. What had been traded for the price of a mansion on the Grand Canal in Amsterdam can now be found in a florist's shop for little more than €20.

Today we know this bubble as the tulip mania; the first documented major financial bubble, but certainly not the last. As the saying goes, man is the only animal that trips twice over the same stone; 400 years later we could read the same story exchanging the word "tulip" for "cryptocurrency", or any other asset that has shone irrationally in this era of excess liquidity.

The tulip mania serves as an example to expose the general cycle of bubbles. From irrational biases and fear of missing out, group mentalities that drive up the prices of an asset to an unsustainable level, to the eventual collapse of those inflated prices. Sooner or later, reality sets in.

As we've mentioned before, Hanway Capital declined to profit from the collapse of this speculative bubble despite warning of it a year ago. We alerted that the return of inflation would force central banks to raise interest rates aggressively, and that this liquidity drain would take a toll on the valuation of the most speculative assets. However, it is never a good idea to try to fight a bubble: the naivety of believing oneself capable of knowing when it will burst is always foolish. Human irrationality is infinite and betting against any asset in a euphoric phase is as reckless, if not more so, than buying it.



Europe dodges General Winter (for now)

The European stock market has experienced one of the best quarters in many years when compared to other indices. While the American stock market has fallen by more than 2% in euro terms, the European stock market has appreciated by 14%. This differential between the two had not been seen since the bursting of the dotcom bubble twenty years ago.

As we constantly underline, the market is a discounting mechanism. The price of assets does not reflect the current state or the future, but rather the evolution of investors' expectations. If we go back to the continent's expectations just three months ago, we were faced with the possibility of an imminent recession, an unprecedented energy crisis, runaway inflation, and a war in full escalation.

But then, without setting a precedent, climate change has worked in the European Union's favor. The non-existent autumn, together with a mild winter, has defeated General Winter (a term used in Russian warmongering rhetoric to refer to winter as its war ally). This winter there will be no blackouts or energy rationing on the Old Continent. The successful plan carried out by the Commission managed to fill gas tanks to 95% before the arrival of cold weather, and the mild temperatures have caused the price of gas in Europe to plummet by 60% since September.

This is how the randomness of Mother Nature has impacted the stock market. If it is not cold and we have plenty of gas reserves the price of energy plummets, the industrial sector can produce without energy cuts and at a cheaper price, which causes inflation to moderate. Where three months ago a deep recession in Europe was taken for granted, most analysts now believe it is avoidable. This has caused a rotation of capital into Europe and the euro.

This battle against Russia has been won by the Union as a result of its quick reaction and planning, but it shouldn't take the victory of war for granted. The gas tanks will start to empty as the cold weather kicks in and by the following winter we will have to refill them for the first time without Russian gas. We must continue to accelerate towards energy sovereignty in the Union and deploy a sensible diplomatic agenda with those countries that can supply us with liquefied natural gas for next winter.

China's reopening

The protests of the Chinese population against Xi Jinping's zero-COVID policies last November have proved effective against all odds. The Chinese government has succumbed to the pressure and in a U-turn has decided to reopen the country after three years of isolation. Up to today, it represents the most important macroeconomic event of 2023.

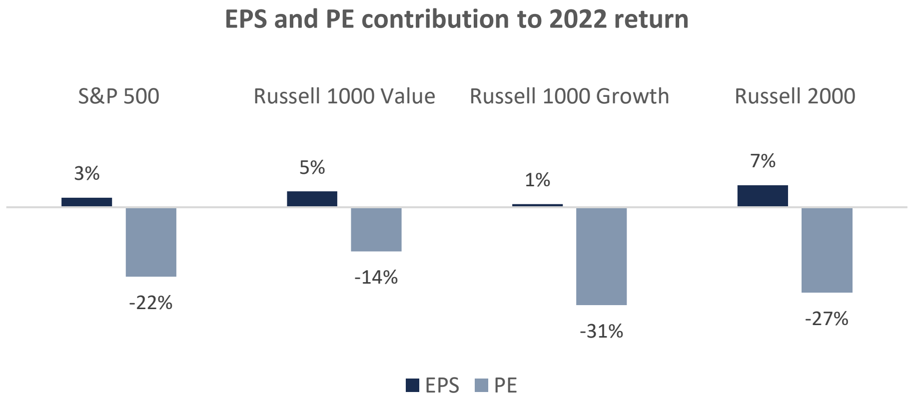
At a time when Western economies are expected to slow down or even enter a recession, the Asian giant will help keep global growth positive. China's macroeconomic reality is very different from that of the West, and with a low inflation of 1.3% they can afford to stimulate the economy with stimulus as already announce by the government.

This is undoubtedly good news for global economic growth and the recovery of supply chains, but it is also a challenge. China is the world's largest consumer of raw materials: it accounts for one-fifth of all global oil consumption and half of all copper and steel consumption. If its economic recovery is strong, a rebound in the price of energy and industrial raw materials is to be expected. At a time when inflation seems to be slowly starting to ease in the West, we could see an upturn that could hamper the work of central banks.

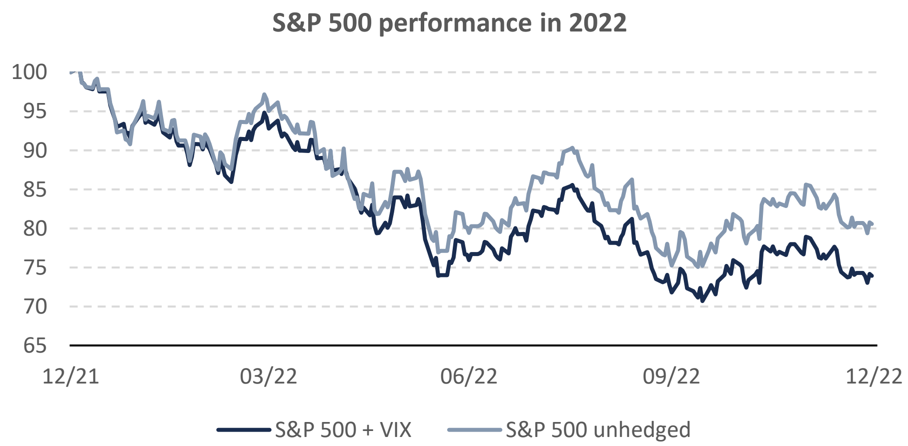
Management report

Let us now analyze the fund's individual positions for this quarter:

1. **Equity positions**: For the fourth consecutive year, and as in 13 of the last 14 years, the world's stock market once again closed the year with a positive last quarter. This helped to offset the negative returns, particularly in the European indices, which saw their losses for the year halved. The US indices, on the other hand, have barely seen any gains if we discount the effect of the falling dollar. Interestingly, the entire equity declines in 2022 are due to a reduction in multiples, as earnings per share have risen. If a slowdown in the economy eventually comes, therefore, equities still have room for further declines. Our presence in the asset has subtracted **-1.3%** from our performance.



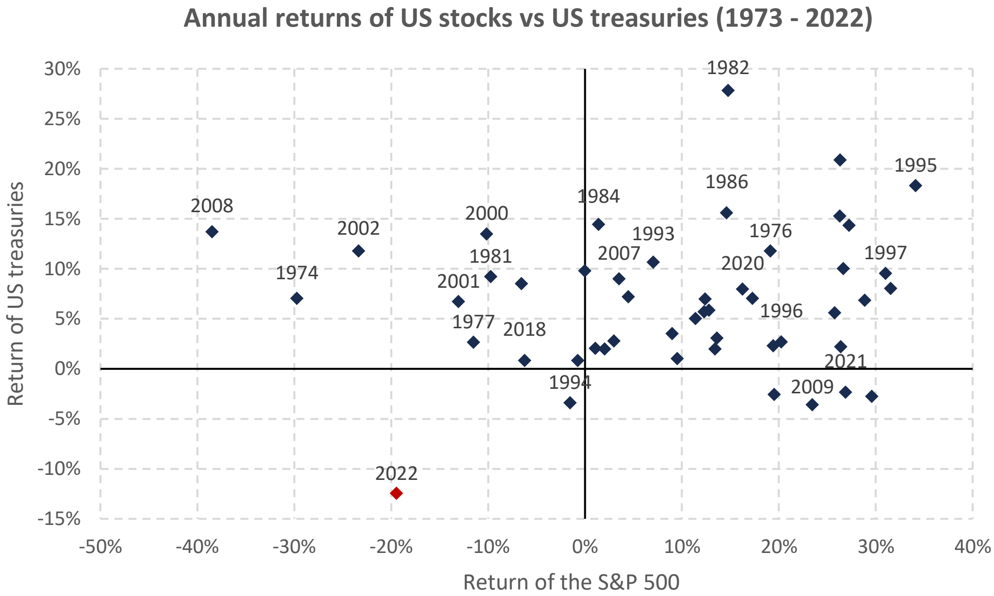
2. **Volatility positions**: The rebound in equities has driven volatility to close 2022 at its lowest level in 12 months. It is certainly surprising that the VIX index has closed the year where it started given the significant declines we have witnessed in stock markets. While in the COVID crisis this asset was the perfect hedge, in the face of war and inflation its performance has been miserable. Incredibly, if a fund used volatility as protection during this year, it has done worse than one that did not protect itself at all; it's as if in a head-on collision the car's airbag accentuated the blow instead of cushioning it. This position has reduced our results for the quarter by **-2.3%**.



3. **Precious metals:** The fall of the dollar this quarter has greatly helped gold, which has managed to erase all the fall accumulated in the year. The latest inflation data, below market expectations, has led investors to assume that the end of interest rate hikes is near. It seems to us that the market is underestimating the commitment of central banks, which will not slow down until they are convinced that price rises have fully stopped. However, precious metals would help us if we were wrong or if inflation recedes faster than we expect. This asset has added **+0.8%** to the result.

4. **Commodities:** While waiting on the impact of China's reopening, commodities have had an inconsequential quarter. We have recently slightly increased our exposure to this asset, in line with our conviction that the real economy will perform better than expected in 2023. During these months, this position has weighed on our performance by **-0.5%**.

5. **Short position in fixed income:** If there was one specific warning we issued in 2021, it was that in the face of an inflation crisis, fixed income was going to fall in tandem with equities. Looking back over the last 50 years, this has been the first in which both the S&P 500 and the government bond index have fallen by more than 10%. Despite that, we believe fixed income has room to fall further, as we believe the Federal Reserve will raise rates to at least 5% and will not lower them until 2024 at the earliest. Our conviction in this position therefore remains intact, and this quarter has added **+1.3%** to the overall result.



"I can calculate the motion of heavenly bodies, but not the madness of people"

- Sir Isaac Newton

Regards,
Hanway Capital

Appendix: Hanway Capital Fund historical returns

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2019	-	-	-	-	-	-	-	-	-	-	-0.4%	1.2%	**0.8%**
2020	-2.9%	-3.0%	18.3%	4.6%	-0.4%	3.2%	-2.3%	0.5%	-2.7%	-1.9%	9.1%	3.8%	**27.0%**
2021	-1.9%	2.8%	3.0%	1.2%	0.6%	0.9%	-0.8%	1.5%	-1.1%	2.4%	1.3%	3.1%	**13.7%**
2022	-1.7%	0.0%	2.1%	1.8%	0.8%	-6.1%	3.0%	2.6%	2.1%	1.9%	-2.2%	-1.7%	**2.0%**

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