

LYNX PROGRAM 2022 REVIEW

LYNX

Summary

The Lynx Program was solidly profitable in 2022, generating a 36.8% rate of return net of fees,¹ as gains were realized across asset classes, model families and timeframes. The yearly result was the second strongest in the history of the program and brings annualized net performance since inception to 10.2%¹ with an annualized standard deviation of 14.8%.¹ The return far surpassed the Société Générale CTA Index (a leading industry benchmark) which ended the year up 20.1%.² And perhaps most importantly, the program provided a needed ballast in diversified portfolios during a year when both equities and fixed income suffered: the MSCI World Index ended the year down 16.3%² while the JPM Global Bond Index lost 13.0%.²

With inflation reaching levels unseen in over a generation, stocks and bonds simultaneously collapsed in the first half of 2022 as investors revised expectations of monetary and fiscal policy. At the same time, commodities rocketed higher fueled by geopolitical conflict in Ukraine as sanctions on Russian exports and a ravaged Ukrainian infrastructure led to speculation that energy and grain supplies would fall well short of demand. However, financial and commodity markets retreated from their extreme levels as the year progressed. Stocks and bond prices fluctuated widely with changing sentiment, while energy and grain prices ultimately ended the year not far from where they began. The program adapted to the changing market environment, generating substantial gains as the crisis escalated before becoming more tactical as prices consolidated.

Full year result¹

36.8%

Lynx Program total assets

7.4 bn
USD

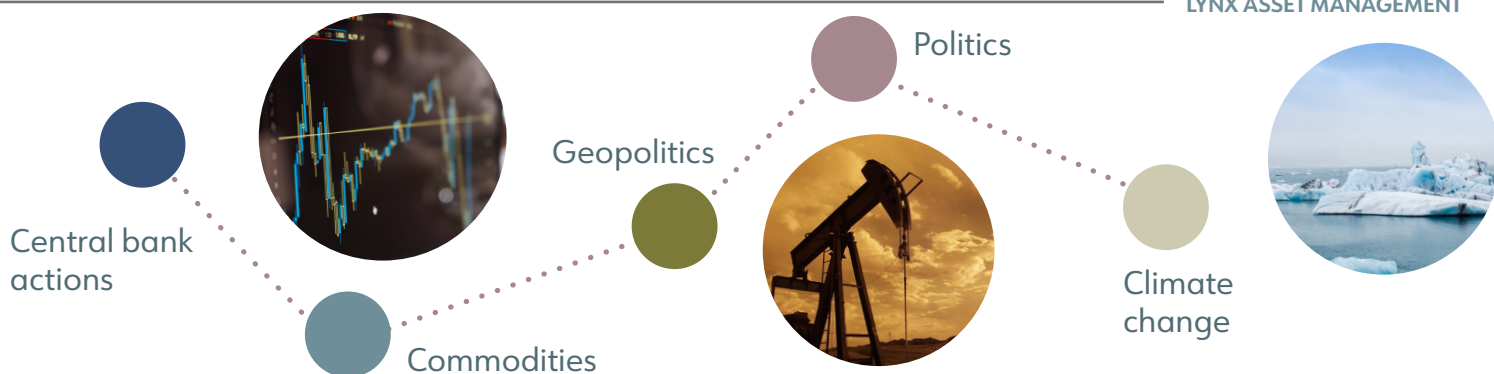
Annualized performance
since inception¹

10.2%

Annualized standard
deviation¹

14.8%

¹ The net performance figures include interest, costs and fees and reflect the standard leverage Lynx Program with a 1% management fee and a 18% (20% up until 1 July 2018) performance fee for a USD investment. For the period 1 May 2000 up until 31 March 2004 pro forma numbers have been calculated based on a SEK investment and thereafter an equivalent investment in USD. ² Index-figures are based on available data at the time of publication and are subject to revision. The Société Générale CTA Index figures represents the period 31 December 2021 to 31 December 2022. The MSCI World NDTR Index (local currency) and the JP Morgan Global Government Bond Index (local currency) figures represents the period 30 December 2021 to 30 December 2022.



Market Developments

2021 was a welcomed change for most investors following the extraordinary events of the prior year. Monetary and fiscal stimulus contributed to record high equity prices and relatively subdued financial market volatility. While inflationary pressures began to build, investors and policy makers largely attributed the heightened readings to what they believed were transitory factors relating to COVID-19. Increases in consumer prices were measured off pandemic lows and supply chain disruptions were expected to diminish as economies and borders reopened. With the benefit of hindsight, we now know that those assumptions were misguided as 2021 proved to be just the calm before the storm.

2022 marked a true departure from what had been status quo as after years of exceptionally accommodative monetary policy, the tide turned dramatically. Inflation reached the highest level across the developed world in forty years and remained stubbornly elevated as the year progressed. Central bankers, quickly realizing they had gotten behind the curve, aggressively began tightening policy. Bond and equity markets simultaneously declined as investors responded to the sudden pivot, with each asset class experiencing their worst start to a year in over half of a century. While tighter financial conditions weighed on growth and recessionary fears began to emerge in the second half, policy makers remained steadfast in their commitment to price stability. Nevertheless, markets vacillated as investors considered how much pain central banks would ultimately be willing to inflict on their constituents.



Central bank actions

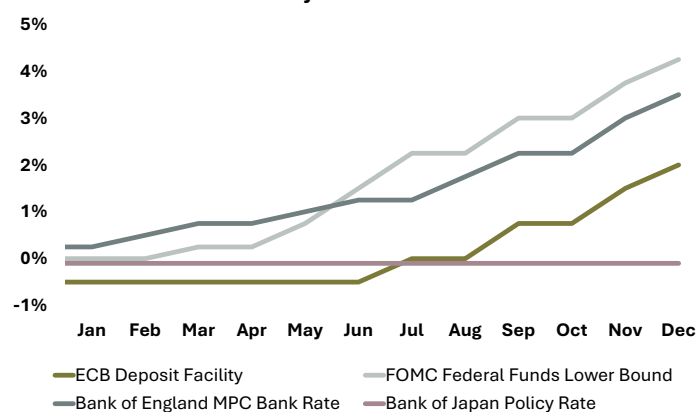
During the height of the coronavirus outbreak in the US, the Fed cut the lower bound of their target lending rate to zero where it remained for two years. Then in March 2022, they began tightening policy for the first time since the pandemic. Before the year was through, the FOMC had hiked rates seven times for a total of 425 basis points – including four consecutive 75 basis point moves – the largest annual increase since 1980. Over the previous 22 years, the policy rate had only risen in 25 basis point increments. In June, they also began reducing their balance sheet of Treasuries and mortgage-backed securities, further tightening financial conditions.

On the other side of the Atlantic, the European Central Bank (ECB) had not raised interest rates in over 11 years by the time they tightened policy in July for the first time in 2022; before the year concluded, the rate of their overnight deposit facility had climbed from -0.5% to 2%. While the pace lagged the US, ECB President Christine Lagarde indicated that the bank was determined to achieve their 2% inflation objective and that significant increases should be expected in the future. Additionally, the Governing Council decided to end net asset purchases in July and announced their intention to begin decreasing the ECB's balance sheet in March 2023. Across the rest of the continent, the Swiss National Bank increased rates for the first time in 15 years, while other central banks hiked dramatically off their post-COVID lows to combat double-digit inflation.

In the UK, the Bank of England (BoE) raised the sterling overnight lending rate by over 300 basis points beginning in February and the resulting increase in gilt yields had unintended and undesirable consequences. The controversial "mini budget" proposed in September after Liz Truss succeeded Boris John-

son as British Prime Minister exacerbated inflationary concerns resulting in a sharp spike in bond yields. Pension schemes in the UK following a liability driven investing (LDI) strategy suffered heavy losses on interest rate derivative positions linked to gilt prices and margin calls resulted in a vicious downward spiral in prices. Ultimately, the BoE intervened to stabilize the market, although rates remained elevated until significant policy changes were announced in October.

Global Central Bank Policy Rates



Source: Each Central Bank respectively

In Asia, the Bank of Japan (BoJ) initially bucked the trend of most other global central banks, maintaining highly accommodative monetary policy even as inflation was climbing. In December, however, they unexpectedly lifted their government bond yield curve control range by a quarter of a percent as the depreciation of the yen was exacerbating price pressures and direct currency intervention during the year had done little to stem its decline. The Japanese currency responded, although most economists speculated that the bank would need to take additional action as CPI ended 2022 at a 40-year high. While inflation remained relatively muted in China as domestic demand was impacted by the government's response to the COVID pandemic, many other Asian nations experienced significantly higher consumer prices as weakening foreign exchange rates pushed up import prices and higher energy costs took a toll.

As growth declined with tighter financial conditions, speculators began to expect central banks to pivot. This unfounded optimism was repeatedly met with definitive comments from central bankers that they would not bend to the will of investors, but rather stay true to their stated objectives. Despite their aggressive actions, inflation remained elevated even as growth forecasts fell. The gross domestic product (GDP) in the US contracted in the first two quarters of the year, technically putting the nation in a recession, although most economists disagreed with that categorization since employment remained robust and corporate earnings continued to grow. However, many of those same economists began forecasting recessions in the US, Europe and elsewhere across the globe in early 2023.

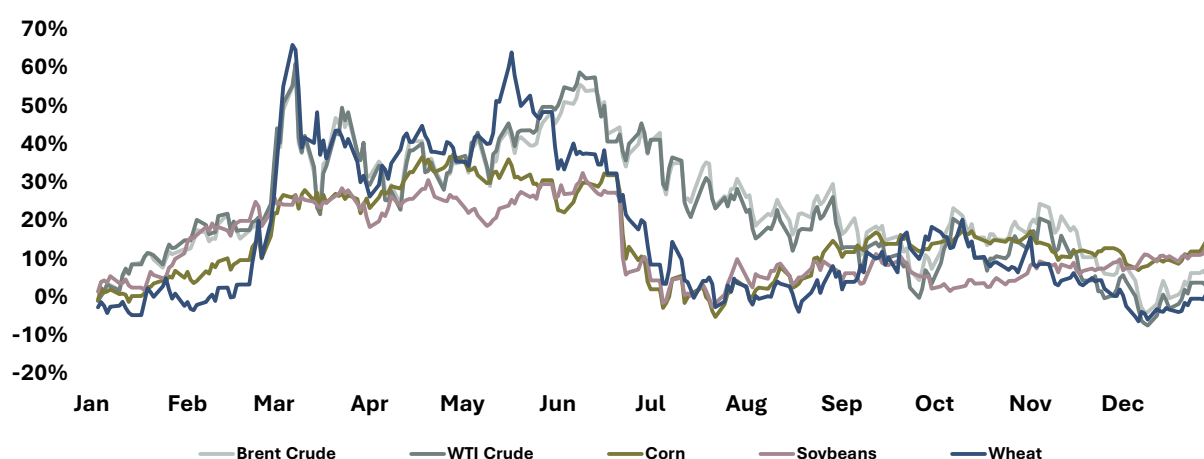
Commodities

The increase in inflation was partly due to significantly higher commodity prices, particularly in the first half of the year. Energies were already climbing entering January but spiked considerably following the Russian invasion of Ukraine in late February. Half of Russian crude oil and three quarters of natural gas exports had been delivered to Europe in 2021, but a series of trade sanctions limited the transfers in 2022. Supply concerns were exacerbated after an explosion believed to be sabotage damaged Nord Stream pipelines under the Baltic Sea signifi-

cantly reducing the potential flow of natural gas to Western Europe which had already been halted in August due to supposed mechanical issues. Remarkably, energy prices retreated as the year progressed, ultimately surrendering previous gains as recessionary pressures outweighed supply concerns. A smaller-than-expected production cut by OPEC+ nations in October and anemic Chinese demand due to COVID-related shutdowns were also contributing factors to the decline.

In other commodities, grains similarly began the year sharply higher on concerns that the conflict in Ukraine would result in a significant supply shortfall. Russia and Ukraine are each major agricultural producers, having accounted for around 30% of wheat and 20% of corn exports in the three years before the invasion, so fears of food shortages appeared warranted. However, farmers in the Americas were able to increase production and carryover stocks from previous harvests were able to bridge the gap until new supply was available. In the metals, a dislocation in nickel was notable as a phenomenal short squeeze catalyzed by the conflict in Ukraine drove prices up 250% from where they were immediately before the invasion. The unprecedented decision by the London Metal Exchange (LME) to cancel trades and suspend trading until balance was restored was highly controversial and continues to be examined by the court system.

Crude oil and grains price development during 2022



Source: Bloomberg



Geopolitics

The conflict in Ukraine had a tremendous impact from a variety of perspectives, not only on the markets. The humanitarian cost has been devastating as tens of thousands have lost their lives and millions of others displaced from their homes. The infrastructure in the country has been ravaged and will likely take years and huge investments to rebuild. The geopolitical balance which endured for decades following the collapse of the Berlin Wall has been disrupted and the relationship between Russia and West could remain dysfunctional for years to come. The financial implications have also been significant. Sanctions on Russia will likely remain in place until Putin withdraws troops from Ukraine and concedes claimed territory in Crimea and the Donbas region or is no longer leading the nation. Export controls have made it necessary for countries to develop new supply chains for natural resources, products, and materials, while energy security became a significant concern around the globe.

Elsewhere, heightened geopolitical tensions between China and the US (and their Asian allies) regarding the sovereignty of Taiwan were perhaps influenced by the conflict in Ukraine. In August, the then-Speaker of the US House of Representatives, Nancy Pelosi, visited Taiwan despite warnings from Beijing that her visit could result in "very serious developments and consequences." The frequency of military exercises in the region increased as both sides exhibited their capabilities and risk of escalation was high as the year came to a close.

Politics

On the political front, Liz Truss became the shortest tenured prime minister in UK history, lasting only 50 days in office. The controversial “Growth Plan” introduced under her stewardship to the House of Commons generated significant concern as economists forecasted higher government borrowing due to significant tax cuts for corporations and the wealthiest individuals. In the US, midterm elections resulted in a divided Congress as Democrats unexpectedly maintained control of the Senate but lost their majority in the House of Representatives to the Republicans. As the new congresspeople would not begin serving until the beginning of 2023, there was a flurry of activity as the year came to a close including the passing of a US \$1.7 trillion appropriations bill to keep the government funded through September and the conclusion of the January 6th Committee’s 18-month investigation into the Capitol riot in 2021 resulting in the referral of Donald Trump to the U.S. Department of Justice for prosecution.

Climate change

On the environment, multiple international organizations focused on climate change sounded their most dramatic alarms to date regarding global warming. The Intergovernmental Panel on Climate Change (IPCC) warned of the consequences should greenhouse gas emissions not decline dramatically by 2030, while the World Meteorological Organization (WMO) estimated that the global mean temperature in 2022 was approximately 1.15° C

above preindustrial levels. Historic floods in Pakistan impacted one third of the nation decimating much of the infrastructure in impacted areas, while deadly flooding also spread across India, Afghanistan, Nigeria, South Africa and Brazil. On the other extreme, drought conditions in the Western US set records for both duration and coverage, while East Africa experienced what the UN deemed “the worst drought in over 40 years.”



Performance attribution

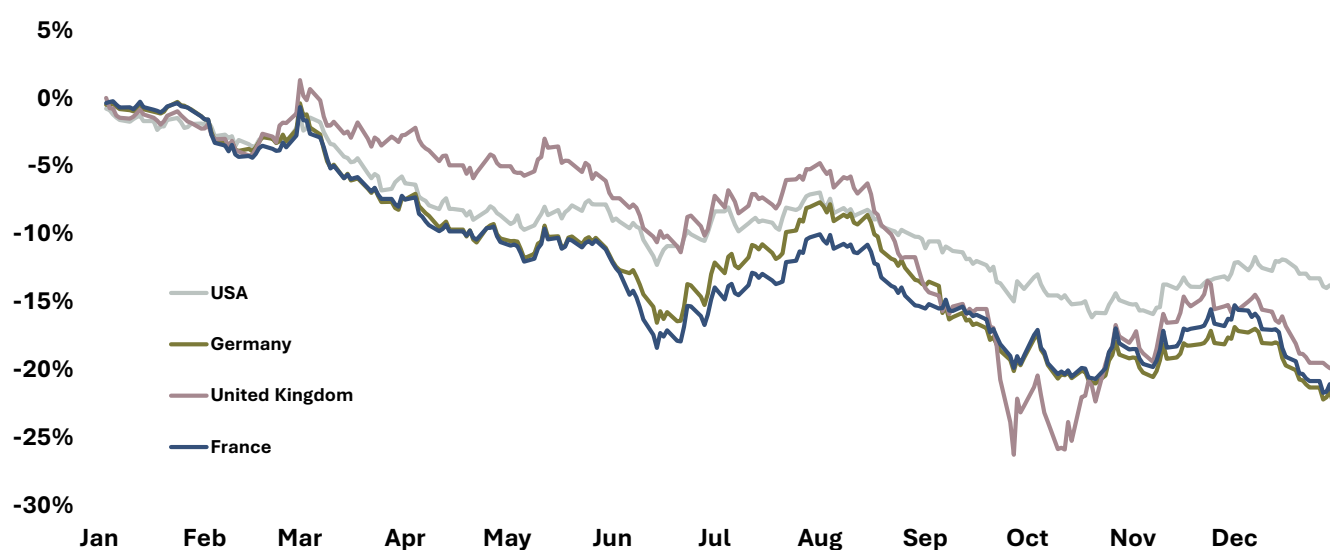
The Lynx Program was strongly profitable in 2022, generating a 36.8% rate of return net¹ of fees as gains were realized in every asset class traded in the portfolio. Trend-following and diversifying models each contributed positively generating profits across timeframes.

Fixed income
26.1%³

Fixed income was the strongest asset class in the portfolio during the year, producing a gain of 26.1%.³ Bonds and short-term interest rates were both profitable, contributing 17.6 and 8.5%,³ respectively. Increasing inflation, normalizing monetary policy, and quantitative tightening all contributed to extraordinary moves in global interest rates. Entering the year with a slightly net long bond position, the program quickly reversed exposure and prospered as rate expectations

climbed sharply in the first half of the year. Solid gains were realized in both Europe and the US, with short exposure in Germany yielding the strongest profits. In early summer, increasing concern regarding global growth and speculation that the Fed may slow the pace of interest rate hikes resulted in a significant pullback in rates and a reversal of the net short bond position. However, the long exposure was short lived as prices again declined after the Fed indicated that policy changes might cause “some pain to households and businesses.” Both trend-following and diversifying models were profitable in the asset class, with trend models capturing gains across timeframe. Amongst the diversifying component of the portfolio, short and medium-term models were positive, while long-term models underperformed.

North American and European 10 year Government Bond performance



Source: Bloomberg

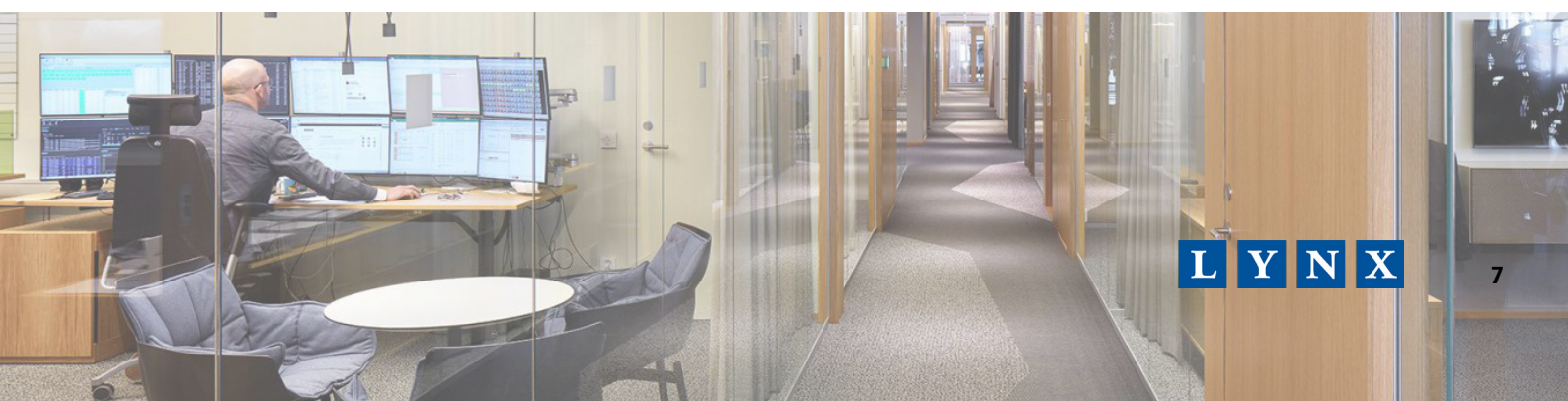
³ Gross return includes commissions and trading expenses, but excludes management fee, performance fee and interest income. When reviewing gross return figures please compare with the total performance figures presented net of fees on pages 1 and 6.

Commodities 7.8%³

Commodities were the second-best performing asset class, generating a gain of 7.8%.³ Energies were particularly profitable due to gains in the first half of the year, as a more challenging trading environment developed in the second half. Prices spiked following the invasion of Ukraine as sanctions on Russian oil and gas led to concerns that Europe would not be able to source sufficient supply to meet demand. After surging over 50%, oil prices subsequently collapsed as recession concerns emerged and Chinese demand declined due to COVID-related lockdowns; starting January just under US \$80 per barrel, Brent crude climbed to US \$128 immediately following the invasion, only to close the year at approximately US \$86. Outside of energies, the largest positive commodity contribution was in nickel where prices over doubled before the LME cancelled trades and suspended trading. While their actions mitigated the potential return, a solid gain was generated, nonetheless. Trend-following models were profitable across time-frame, while short-term diversifiers underperformed their longer-term counterparts, generating a slight loss.

Foreign exchange 6.6%³

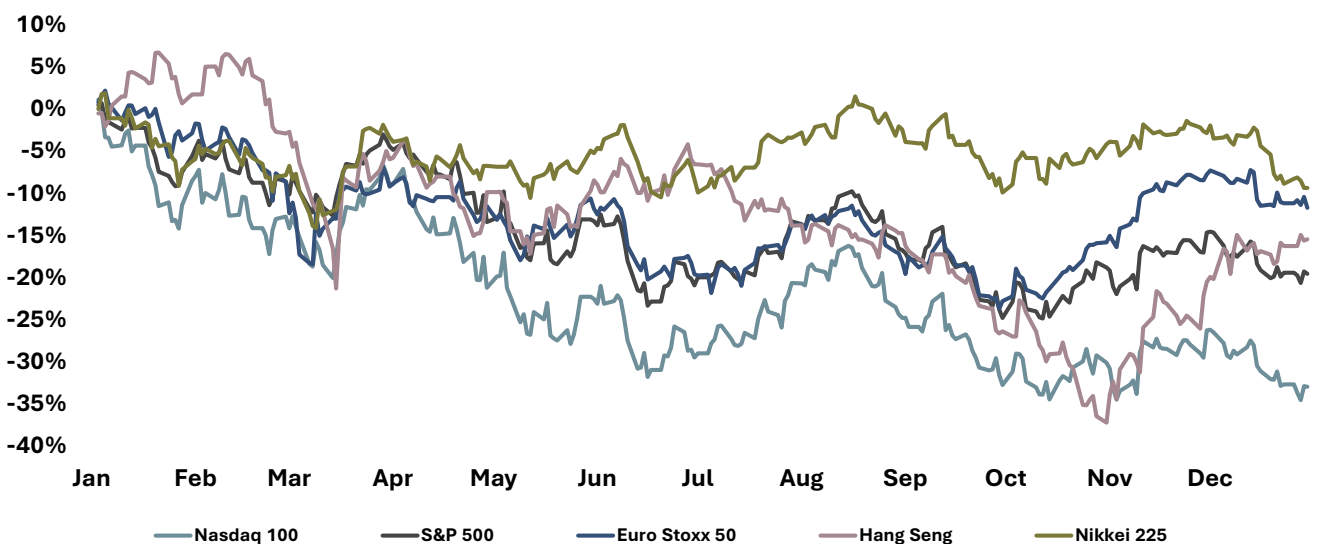
The annual gain in foreign exchange modestly trailed commodities at 6.6%.³ Long positions in the US dollar were primarily responsible for the annual gain as relatively restrictive Fed policy resulted in the greenback strengthening against most developed market counterparts. Largest profits were realized in the Japanese yen as the BoJ remained committed to exceptionally loose monetary policy despite rising inflationary pressures. The yen broke through the 150 level against the US dollar for the first time since August 1990 but retreated soon after on speculation that the Japanese central bank would be forced to pivot. Solid gains were also generated in the euro as the US dollar crossed parity for the first time in 20 years with the ECB lagging the Fed and not tightening policy until July. As with the yen, the euro recovered somewhat in the fourth quarter and the program reversed to a long position in November locking in previous gains. Notable profits were also realized in the British pound, Swedish krona, Mexican peso and New Zealand dollar, while largest losses were generated in the Canadian dollar and South African rand. Gains were generated by trend-following and diversifying models, with only short-term diversifiers producing a small loss.



Equity indices
2.7%³

Finally, equities trailed other asset classes with a 2.7%³ gain as significant long positions entering the year resulted in early losses as global bourses collapsed on increasing inflationary pressures and geopolitical tensions. However, the program quickly reversed exposure and captured solid profits as markets continued to trade lower as the year moved forward. Models responded as prices vacillated on shifting expectations of monetary policy, building long positions in August and December, but ultimately ended the year with net short exposure. Trading gains in Asia far surpassed those in Europe or the US, although losses in Japan were a notable exception. Short positions in China were particularly profitable as equity indices in Hong Kong and mainland China declined sharply on speculation that Xi Jinping would be emboldened in his efforts to rein in corporate profits after securing his third term as China's "core" leader. Unlike other asset classes, model performance was mixed in equities as gains in diversifying models offset losses in trend-following. Long and medium-term trend models were especially challenged by the price reversals during the year, while machine learning and implicitly long volatility models performed particularly well.

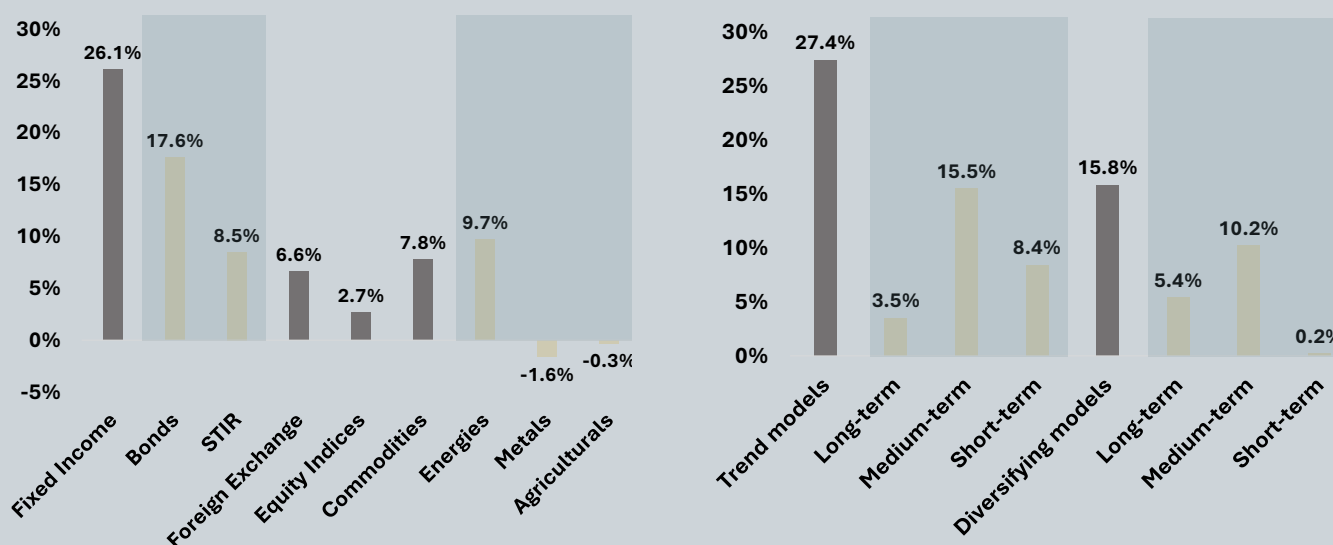
Global Stock Index performance



Source: Bloomberg

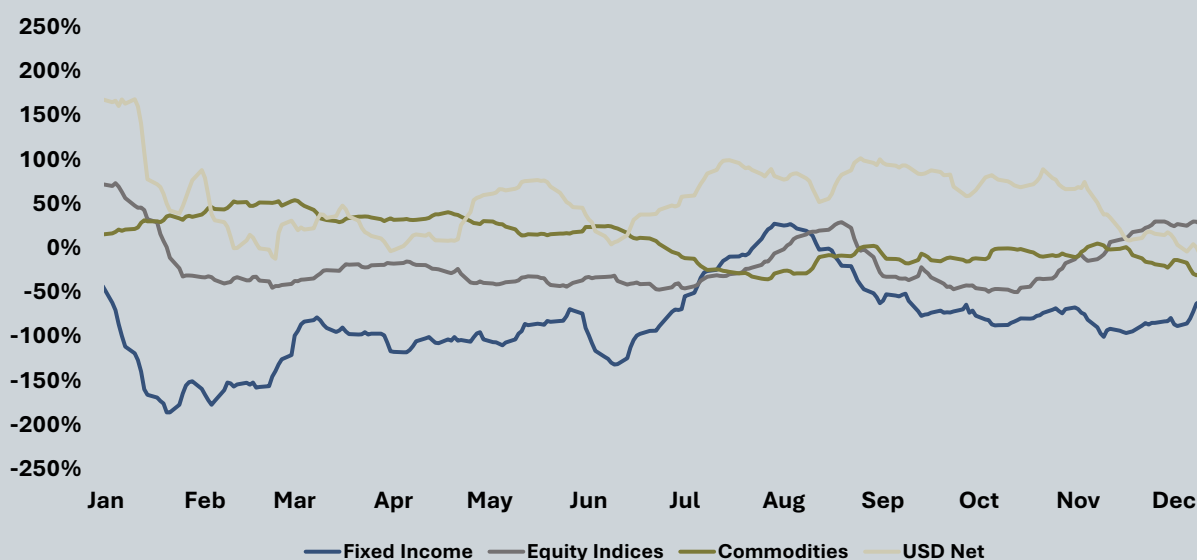
Performance and exposure summary

The charts below show a summary of gross returns³ by asset class and model category, respectively and as well our net exposure by asset class⁴ during the year 2022.



Source: Lynx Asset Management AB

Net Exposure by Asset Class in 2022



Source: Lynx Asset Management AB

⁴ The notional exposures for fixed income markets are expressed as estimates of 10-year equivalents



Outlook

Central banks have remained steadfast in their commitment to fight inflation as the potential longer-term consequences are otherwise too painful. Optimism that these same banks will blink in the face of recession, likely based on over a decade of extraordinarily accommodative monetary policy, is perhaps unfounded as there is no requirement for them to provide a safety net for equity and bond investors.

But what happens next? It is easy to imagine scenarios developing in 2023 that could take markets in either direction. Consumer prices could continue climbing despite tighter policy due to supply-related challenges while global growth and employment rates decline. Traditional monetary policy is ill equipped to tackle stagflation as addressing one side of the imbalance exacerbates the other, so the potential repercussions could be disastrous. Conversely, the lagged impact of higher interest rates on demand could stabilize consumer prices allowing central banks to ease financial conditions later in the year. Equity and bond markets would likely welcome the change of course and prices could rally back beyond previous highs. And while commodity inflation has mitigated in recent months, China's abandonment of their "zero-COVID" policy could result in refreshed demand for raw materials as their economy reopens.

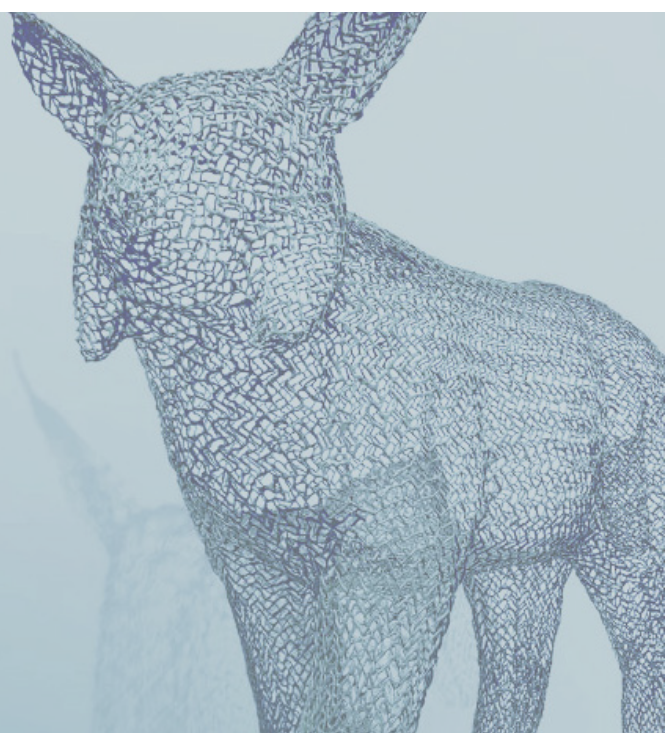
To be sure, there are a multitude of potential scenarios which could develop, and what transpires in one economy may be wholly different from another. A tactical, opportunistic approach with an unbiased global mandate could be in the best position to manage the potential risks and rewards.

There are other factors that should be considered outside of inflation. While we have previously highlighted nationalist policies as a risk to global trade and macroeconomic balances, the conflict in Ukraine has somewhat changed that narrative. "Everyone for themselves" no longer had the same attraction and countries sought to cement military alliances. After generations of neutrality, Sweden and Finland applied to join NATO during the year and many NATO members advocated changing the organization's aspirational, yet rarely achieved, military spending target into a minimum requirement. While globalization appears to be declining, regional and ideological coalitions are strengthening, potentially resulting in shifts in the balance of trade, supply chains and asset flows. The economic isolation of Russia from the West has already led to significant changes, but the financial market impact of future shifts could be dramatic.

Additionally, while energy security seemingly took precedence over the environment in 2022 with coal usage hitting a record high according to the International Energy Agency (IEA), the quest for energy independence could lead to the increasing adoption of alternative power sources going forward. Lynx supports ESG and sustainability initiatives and looks forward to the eventual “green transition” when fossil fuels are replaced by renewable energy. The foundation for this change is firmly in place with substantial government support, particularly in Europe with the EU taxonomy, and strong economic incentives. As nations refocus on the environment, this transition could accelerate and have a tremendous impact on financial and commodity markets alike.

The trends resulting from any of the above catalysts could be extraordinary and we believe that our models would be well equipped to capitalize on them as they develop. Lynx is committed to managing your capital responsibly and profitably. We are grateful for the confidence that you have placed in us and hope to reward that faith with differentiated, positive returns in 2023. We are invested alongside our clients in every program we manage, aligning our interests directly with yours, so you can be sure that we will do our best to reach our potential.

Lynx Asset Management



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