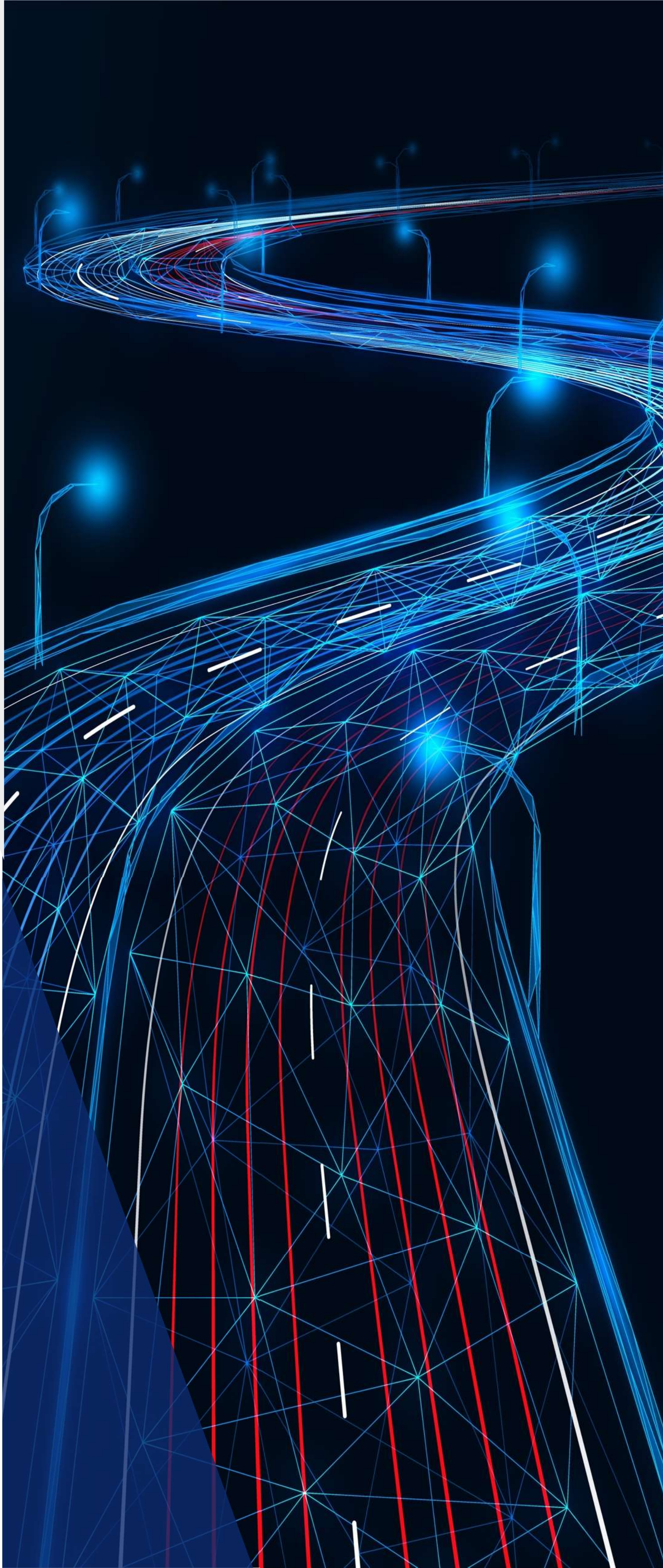
# OPPORTUNITIES IN A VOLATILE MARKET

June 2022



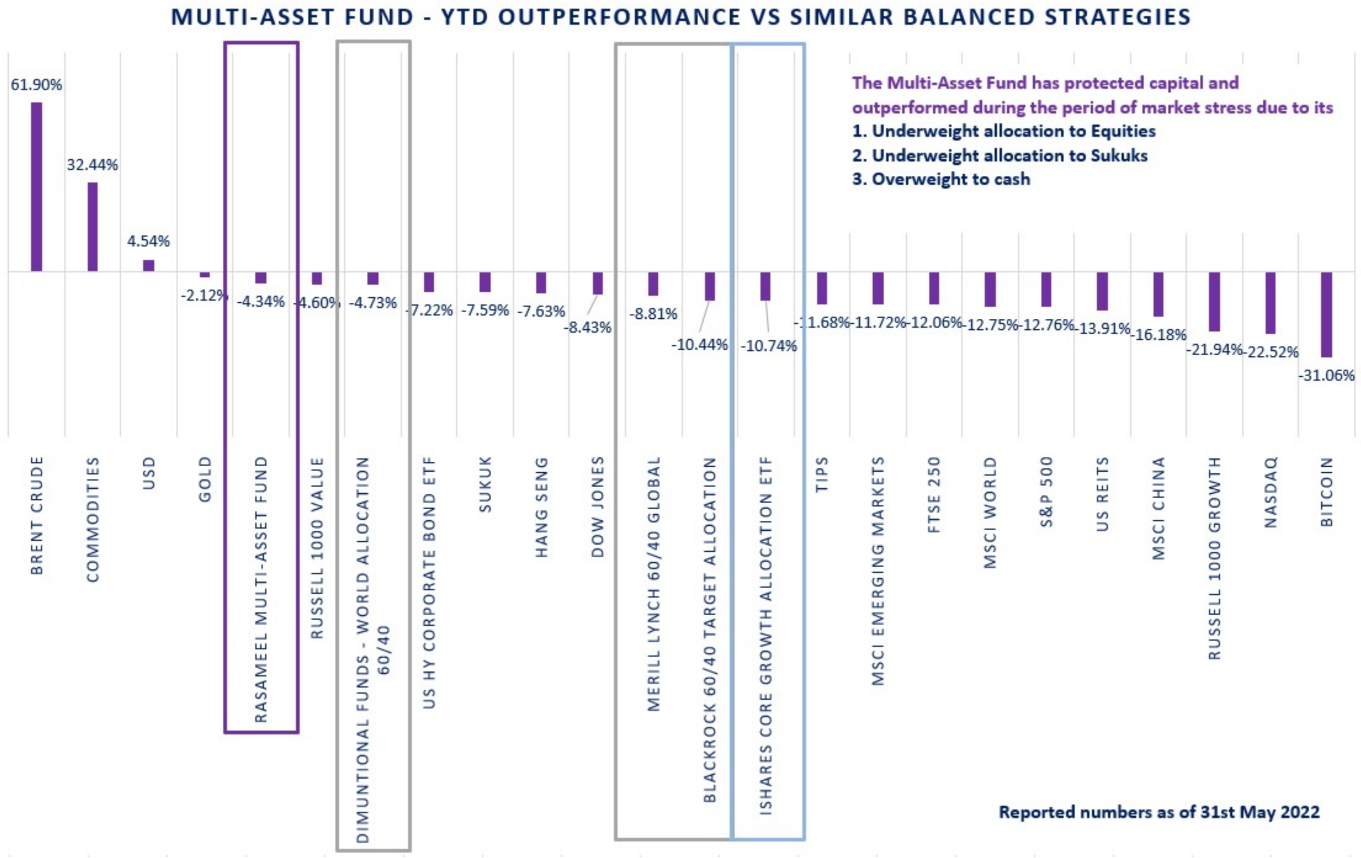
RASAMEEL

## RASAMEEEL'S MARKET UPDATE: JUNE 2022

Our relative outperformance reflects our more cautious outlook coming into the year. YTD, we are outperforming our benchmarks across all strategies. As at the end of May, the Global Strategy was down 4.7% (gross), which compares to both the MSCI World and the S&P 500 down 12.8% over the same period. The Disruptive Technology Strategy is down 17.4%, compared to the XT and ARKK down 21.2% and 53.4% respectively.

**The Muti-Asset Fund is working particularly well YTD to the end of May, down just 4.9% vs its benchmark down 10.7%.** The fund is doing exactly what was intended – it navigated the sell off as well as could be expected and is well positioned to capture upside when the market turns. **Indeed, we consider this product to be the most suited to the environment we see before us – one of significant volatility across asset classes.**

**Muti-Asset – YTD outperformance VS similar balanced strategies**




As readers of our factsheets and updates will note, we have been effective at preserving capital into declines and generating strong returns, coming out of sell offs. 2020 is a good example of this, where we cut early on, minimizing the drawdown, and were up 21% at the end of the year, well ahead of the index which was only up 7.8%.

Indeed, buy low, sell high, adding exposure during testing times, when sentiment and markets are weak, is the right strategy. So, **we would urge readers to use these periods of market weakness to average in and look to add exposure should we get a larger selloff and/or when we give the signal.**

Indeed, we do find opportunistic areas to add to across the strategies and have done so. That's our valuation bias. Our macro-overlay though, signals we need to cut back overall risk exposure. So, we have added to areas we think are oversold and should find some support, and cut back on wider market exposure, reducing names we think will perform poorly within a weaker economic environment.

**This rest of this update is broken into three sections:**

- **Market update as of June 10th 2022**
- **Our rationale for adding marginally to select Equity names:**
  We added very selectively to a few equities at the end of May, in the view that they were very sold down and offered value. They are names that are largely less dependent on economic growth so should do fine within a slower economy.
- **Our risk management process and rationale for cutting overall risk exposure now on concern that we may be entering a wider bear market – always difficult to time – and the steps we will take to further reduce drawdowns if the case.**

## PART 1: MARKET UPDATE: JUNE 10TH

It's been a wild ride in the market year to date. Equities have been hammered, with major indices such as the S&P 500 and NASDAQ down 18% and 27.5% respectively YTD. The Nasdaq was down 30% at its trough on 20th May 2022. It hasn't just been equities. Bonds have also been hammered, with the 10-year yield having risen from 1.5% at the start of the year to 3.16% currently. The two-year yield has ramped from 15bps a year ago, to just over 3% today. Bond indices are down 7% for the year. Precious metals also got hit lower, particularly silver down 6%.

Pretty much everything is down YTD. Except obviously for those commodities that have been impacted by the conflict in Ukraine, most notably agricultural commodities and energy.

**Equities – as on 10th June 2022**

| Index | RMI | 2Day | Value | Net Chg | %Chg | Δ AVAT | Adv/Dcl | P/E | Est FY1 | Est FY2 | DvYld | %YtdCur |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1) Americas | | | | | | | | | | | | |
| 11) DOW JONES | | | 31392.79 | -880.00 | -2.73% | -3.50% | 1/29 | 16.91 | 16.40 | 14.90 | 2.10 | -13.61% |
| 12) S&P 500 | | | 3900.86 d | -116.96 | -2.91% | +4.15% | 35/468 | 19.50 | 17.08 | 15.65 | 1.64 | -18.16% |
| 13) NASDAQ | | | 11340.02 | -414.21 | -3.52% | +1.33% | 687/2769 | 37.51 | 23.87 | 20.06 | 0.89 | -27.52% |
| 14) S&P/TSX Comp | | | 20274.82 d | -289.07 | -1.41% | +2.44% | 48/190 | 15.75 | 12.51 | 12.07 | 2.88 | -5.51% |
| 15) S&P/BMV IPC | | | 48471.52 d | -818.70 | -1.66% | -44.25% | 1/34 | 13.77 | 12.58 | 11.47 | 3.61 | -6.42% |
| 16) IBOVESPA | | | 105481.23 d | -1612.48 | -1.51% | +12.47% | 11/81 | 5.72 | 6.06 | 6.29 | 9.20 | +12.42% |
| 2) EMEA | | | | | | | | | | | | |
| 21) Euro Stoxx 50 | | | 3599.20 d | -125.25 | -3.36% | +97.83% | 2/48 | 13.52 | 11.45 | 10.96 | 3.48 | -22.55% |
| 22) FTSE 100 | | | 7317.52 d | -158.69 | -2.12% | +22.29% | 10/90 | 16.77 | 10.18 | 10.10 | 4.11 | -9.79% |
| 23) CAC 40 | | | 6187.23 d | -171.23 | -2.69% | +18.09% | 1/40 | 13.49 | 10.89 | 10.79 | 3.11 | -19.99% |
| 24) DAX | | | 13761.83 d | -436.97 | -3.08% | +18.70% | 1/39 | 12.37 | 11.41 | 10.66 | 3.39 | -19.86% |
| 25) IBEX 35 | | | 8390.60 d | -320.60 | -3.68% | +102.80% | 0/35 | 12.38 | 11.56 | 10.76 | 3.56 | -10.93% |
| 26) FTSE MIB | | | 22547.48 d | -1229.49 | -5.17% | +116.39% | 0/40 | 12.01 | 8.56 | 8.01 | 5.19 | -23.73% |
| 27) OMX STKH30 | | | 1990.80 | -53.26 | -2.61% | +15.70% | 3/27 | 14.44 | 15.35 | 13.70 | 4.92 | -25.72% |
| 28) SWISS MKT | | | 11084.62 d | -237.81 | -2.10% | +21.12% | 0/20 | 15.09 | 16.05 | 14.33 | 2.98 | -20.45% |
| 3) Asia/Pacific | | | | | | | | | | | | |
| 31) NIKKEI | | | 27824.29 d | -422.24 | -1.49% | +2.27% | 34/189 | 19.78 | 15.64 | 14.64 | 1.99 | -17.26% |
| 32) HANG SENG | | | 21806.18 d | -62.87 | -0.29% | +19.81% | 22/42 | 7.86 | 11.16 | 9.63 | 3.06 | -7.43% |
| 33) CSI 300 | | | 4238.99 d | +63.32 | +1.52% | +44.33% | 241/53 | 15.99 | 13.53 | 11.56 | 1.86 | -18.71% |
| 34) S&P/ASX 200 | | | 6931.98 | -87.77 | -1.25% | +4.03% | 18/179 | 16.10 | 14.04 | 13.58 | 4.74 | -9.68% |

**Commodities - as on 10th June 2022**

| Commodity | 2Day | Price | Norm Chg | %Chg | Δ AVAT | Time | %YTD | %YTDCur |
|---|---|---|---|---|---|---|---|---|
| 1) Energy | | | | | | | | |
| 2) NYM WTI Crude | | 120.67 | -0.84 | -0.69% | +20.64% | 06/10/22 | +60.44% | +60.44% |
| 3) ICE Brent Crude | | 122.01 | -1.06 | -0.86% | +27.26% | 06/10/22 | +56.87% | +56.87% |
| 4) ICE ARA Gasoil | | 1,281.75 | -26.00 | -1.99% | -95.05% | 06/10/22 | +92.17% | +92.17% |
| 5) NYM NYH Gasoline | | 417.22 | -10.40 | -2.43% | +3.88% | 06/10/22 | +87.22% | +87.22% |
| 6) NYM NYH Heating Oil | | 436.67 | -3.70 | -0.84% | -14.29% | 06/10/22 | +87.40% | +87.40% |
| 7) NYM HH Nat Gas | | 8.85 | -0.11 | -1.26% | -1.54% | 06/10/22 | +137.27% | +137.27% |
| 8) ICE NBP Nat Gas | | 146.24 | -4.37 | -2.90% | +4.23% | 06/10/22 | -14.30% | -22.01% |
| 9) Metals | | | | | | | | |
| 10) LME Aluminum | | 2,680.00 | -81.00 | -2.93% | -- | 06/10/22 | -4.54% | -4.54% |
| 11) LME Copper | | 9,447.50 | -167.50 | -1.74% | -- | 06/10/22 | -2.81% | -2.81% |
| 12) Spot Gold | | 1,871.60 | +23.65 | +1.28% | -- | 06/10/22 | +2.32% | +2.32% |
| 13) DCE Iron Ore | | 906.00 | -14.50 | -1.58% | -95.48% | 18:00 | +45.03% | +37.40% |
| 14) LME Nickel | | 27,264.00 | -759.00 | -2.71% | -- | 06/10/22 | +31.35% | +31.35% |
| 15) Spot Silver | | 21.89 | +0.20 | +0.91% | -- | 06/10/22 | -6.09% | -6.09% |
| 16) SHF Steel Rebar | | 4,735.00 | -51.00 | -1.07% | -78.10% | 18:00 | +1.14% | -4.18% |
| 17) Agriculture | | | | | | | | |
| 18) CME Live Cattle | | 136.20 | -1.00 | -0.73% | -56.14% | 06/10/22 | -1.94% | -1.94% |
| 19) ICE Coffee | | 228.80 | -6.00 | -2.56% | +84.99% | 06/10/22 | +1.24% | +1.24% |
| 20) CBT Corn | | 720.50 | +3.75 | +0.52% | +0.17% | 06/10/22 | +30.34% | +30.34% |
| 21) ICE Cotton | | 122.36 | -2.57 | -2.06% | +84.71% | 06/10/22 | +28.83% | +28.83% |
| 22) CBT Soybeans | | 1,568.25 | -14.00 | -0.88% | +18.24% | 06/10/22 | +31.36% | +31.36% |
| 23) ICE Sugar | | 19.07 | -0.44 | -2.26% | +23.28% | 06/10/22 | -0.05% | -0.05% |
| 24) CBT SRW Wheat | | 1,084.75 | +0.00 | +0.00% | +3.11% | 06/10/22 | +38.92% | +38.92% |

We came into the year expecting that we could see a sell off, anything from 5-15%, given geopolitical risks, rising rates and stretched valuations. It was a brave call to make in a market which had been rallying for some time and we struggled to keep up with equity indices last year, which was very narrow and we didn't want to chase overbought momentum. So, coming into the year we were overweight cash and, in the case of the Muti-Asset Fund, underweight both equities and sukuk.

Throughout the first half of this year, and as highlighted in our Outlook 2022 report, we have been of the opinion that the 2H22 would be one of weaker than expected economic growth and that the eventual recession would only be in 2024. I fear now though, that even this cautious outlook, has been overly optimistic. Given the massive collapse in the Consumer Sentiment data we saw on Friday, down to levels we last saw in 2008, combined with the higher-than-expected inflation data and another fall in the ECRI leading indicator, I fear we may be rapidly falling into a slowdown sooner than we had expected. And this is before the Fed has even really started to tighten.

We haven't yet seen the employment data weaken. Nor manufacturing. But these data points are often lagging indicators, with layoffs starting only as we go through the recession rather than on entry.

At this juncture, I have two main concerns – will the Fed tighten into the likely approaching slowdown, making things worse; and if the economy is as weak as some of the data is suggesting, what on earth can they do about it?

On the first, time will tell. I think they may raise 75 bps in the next meeting just to have some leeway to ease as the economy weakens later in 2H22/2023. Our base case since the start of the year is that inflation and economic data should weaken into the 2H22, thus putting less pressure on them to tighten.

On the second concern is that, even if they raise to 2%, if the economy is as weak as Friday's data suggests, they won't have much fire power to cut and would have to undertake a massive bond buying program later in the year and into 2023. So real rates would have to move into significant negative territory. The level of tightening in financial markets is already significant and the Fed is now truly boxed in. Tighten, and the oncoming recession will be worse. Flip, 2018 style, and provide liquidity and restart QE and things can stabilize. But the inevitable day of reckoning simply gets postponed and inflation will be that much higher for longer (gold would likely move a lot higher as well).

Truly, we live in interesting times. On the one hand, we see some interesting oversold areas in the market that are, in our opinion, worth adding to. On the other, we see a world where inflation is raging globally, central banks are very late in cycle, food inflation and potential scarcity is becoming a topic of concern, particularly as war rages in Ukraine and the West seems destined to enlarge it and China lockdowns and Taiwan tensions capture headlines.

In the past 25 years of my career, I've invested through many bear cycles. They are painful to go through and perseverance and discipline are critical. More critical is to leave emotion out of it and focus on the data. For those that can manage through a difficult market, preserve capital and buy when sentiment is at its lowest, there can be outsized returns.

With this in mind, we have increased our cash allocation by around 5-10% across each strategy. We will reduce risk by a further 5-10% or more, if necessary, should we see key technicals and the underlying data weaken further, or the Fed over tightens. This has been a tough call to make as, unlike 2000 and 2008, the data points are not that easy to interpret, and timing is always tricky.

## PART 2: OUR RATIONALE FOR ADDING MARGINALLY TO SELECT NAMES AS AT THE END OF MAY

As highlighted, parts of the equity market have been heavily sold down, particularly the Nasdaq and similar Tech heavy indices. Indeed, the **XT and the Nasdaq are trading at, or close to, key support levels.** They may well break through but historically the 200wma has offered support and the indices often bounce higher. N

**Chart – iShares Exponential Technologies ETF**

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### Chart – Nasdaq


**Hence, our buys have been primarily in the names we feel:**

- **are less reliant on economic growth and more reliant on the cost of capital, so as to benefit from the eventual FED pivot a little further out, and**
- **have started to reach oversold levels and where the fundamentals are still supportive.**

We recently added to **Facebook (FB US) or META**. The stock is down 54% off its highs and 47% off YTD. Clearly the market didn't like FB's investments in the Metaverse and there is significant concern that this will not generate the sort of growth investors require. Also, there are issues around data security, Apple's IDFA changes etc. But strip away all these concerns, you have WhatsApp and Instagram with c.3 billion active users and these platforms have not been monetized to their full potential. FB itself has a user base of 1.8 billion and while many may dislike the product, it is still an extremely effective marketing platform and highly profitable. The company has a P/E of 14 and c.30bn USD net cash on its balance sheet and is currently in oversold territory.

### Chart – META Platforms as on June 10th 2022

Another is **Zoom (ZM US)**. The stock is down 81% off its peaks and 42% YTD. It's been a 'dog' of a stock. But the fundamentals are still decent with the market expecting revenue and EPS growth over the next few years to be around 10%+, potentially much higher if we have lockdowns again. Something which I consider is very likely as a large part of the world still lives in fear.

The 'covid 19 work from home' boom the stock enjoyed has now been fully wiped out and this is a company sitting on USD 5.5bn net cash. The business model is still relevant, what with an economic slowdown and high energy prices, folks are more inclined to do Zoom calls rather than travel. Yes, there is competition from Teams and Google, but at this valuation, is priced in to a great extent.

**Chart – Zoom as on June 10th 2022**


Another name we have added to is **VIPshop (VIPS US)**, a name we have held for a long while and at current levels is really cheap and we are starting to see China take steps to help the economy avoid a nasty recession.

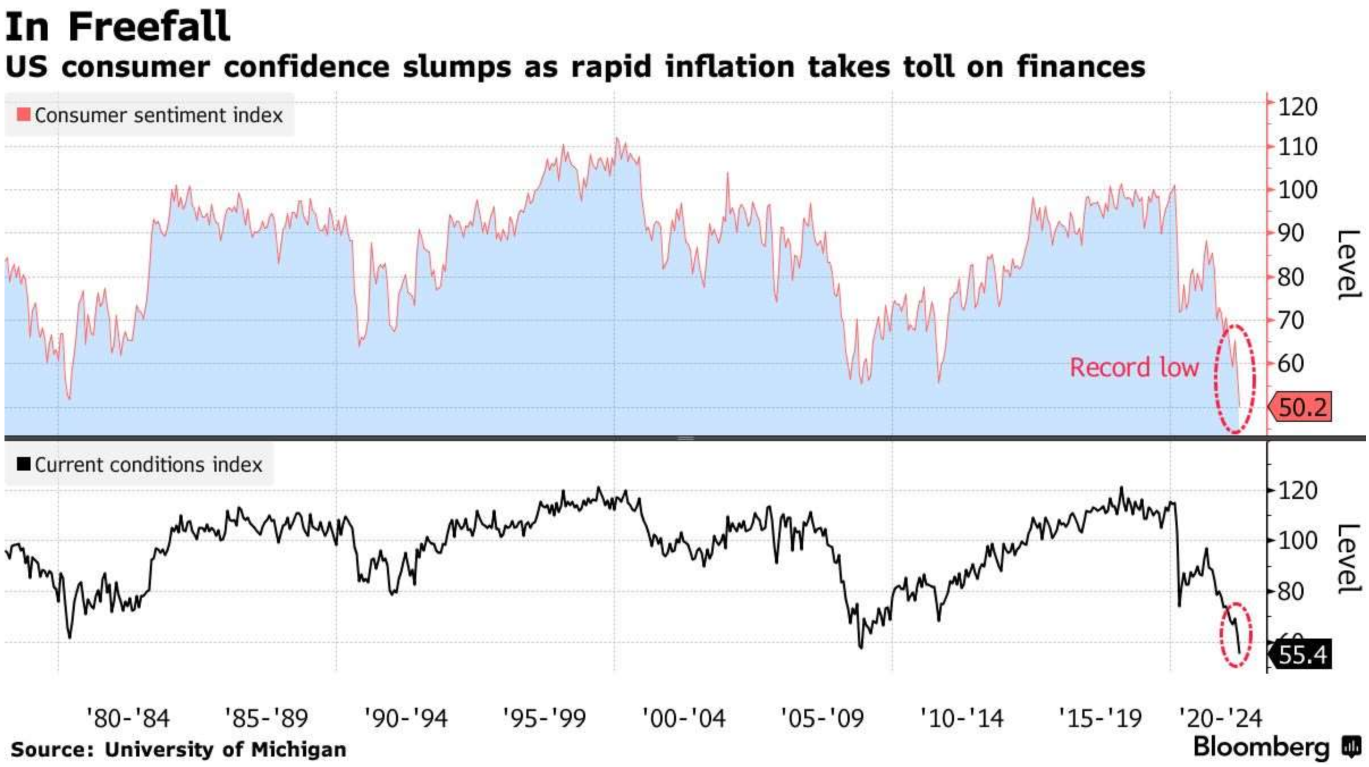
**Chart – VIPShop as on June 10th 2022**

Other names we are adding to across Strategies are **Yellow Cake (YCA LN)**, a uranium ETF and a play on Nuclear power making a comeback. **Globalfoundries (GFS US)**, which is a play on local USA chip manufacture and should hopefully provide some hedge if issues arise with Taiwan supplies, **Twilio (TWLO US)**, a name which has been sold down significantly, but still offers strong growth and has a resilient balance sheet.

**Overall though, we only added opportunistically and very marginally to these names.**

## PART 3: OUR RATIONALE FOR CUTTING OVERALL RISK EXPOSURE ON CONCERN THAT WE MAY BE ENTERING A WIDER BEAR MARKET

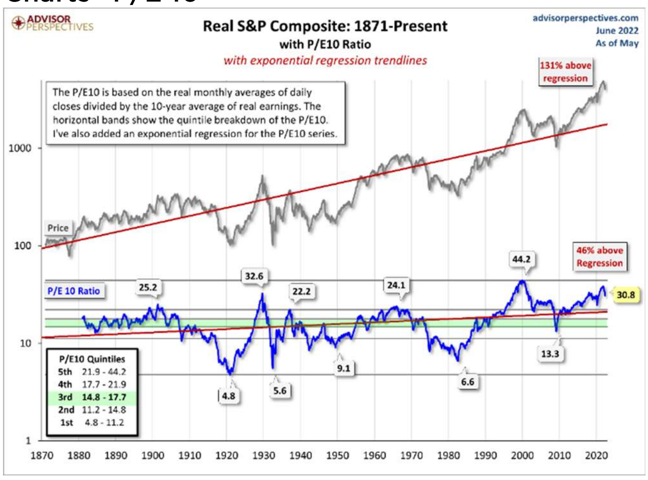
As we note at the start of this update, our decision to cut back on risk exposure at the portfolio level is due to the dramatic drop off in the consumer sentiment data combined with a higher-than-expected inflation read. Whist we have been right relative to consensus on the direction of the market, I fear even our expectations were overly optimistic and it's time to reassess.



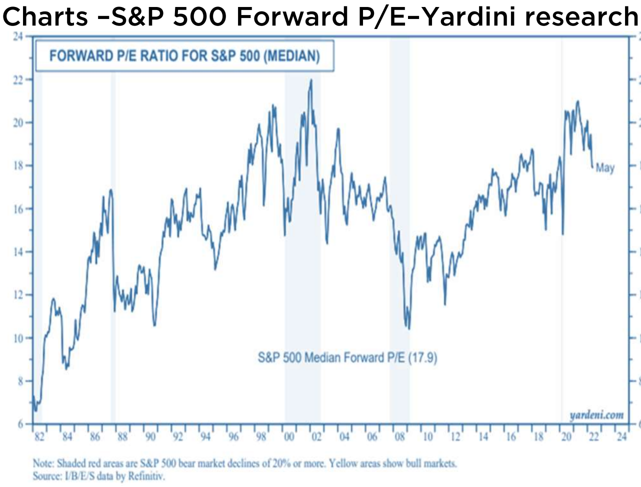
Commentators can argue that this is a bullish signal as it shows that a lot of fear is already in the market. Looking at the indices there is certainly some truth in that. However, looking at margin debt, close to all time highs, and valuations, one would argue that we have to take this indicator very seriously.


In terms of valuations, the market is still trading above median averages for the last few years. Not only that, consensus earnings are also likely to fall in our opinion.

Charts –P/E 10




Charts –S&P 500 Forward P/E–Yardini research




So, on the back of Friday's (10th June 2022) data we decided it prudent to cut risk back. As discussed above, if the Fed comes off the brake earlier than the market currently expects, say July/August, the market will likely stabilize, and certain areas could rally. Then the oncoming recession will be pushed out.

**But if, however, the Fed acts irrationally by 'going Volker' to stem the higher inflation and overtighten they will likely cause dramatically excessive tightening, and the markets will move yet lower.**

**We will take further steps to protect client capital.**

We will use basic technicals, such as if the 50 wma cuts through the 100wma on the downside, and other indicators to decide if we need to cut further. The 50/100wma cross is not perfect as a leading indicator, but we have found that in the last c.20yrs, the indicator worked well.

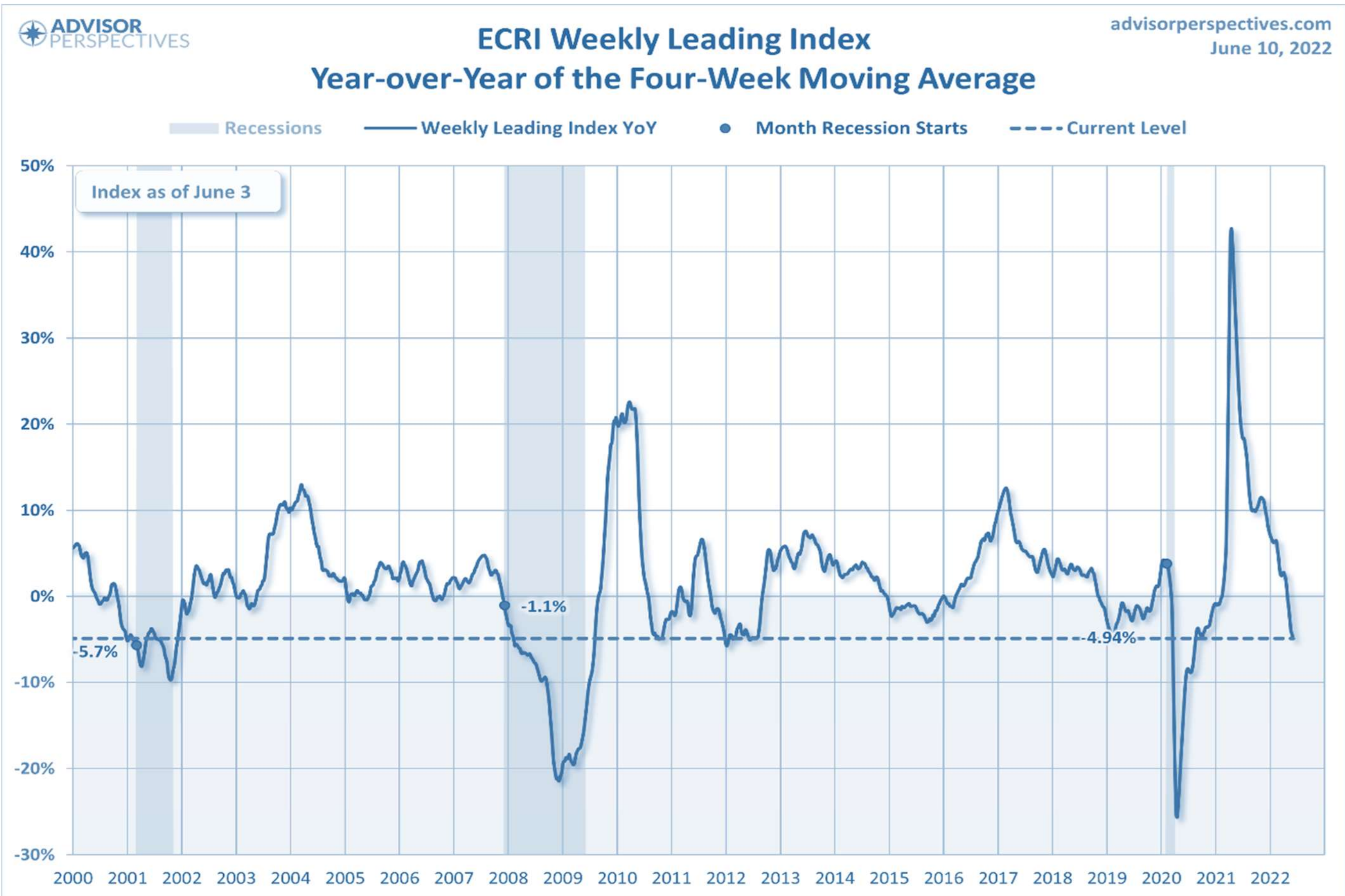
While the indicator worked less well prior to 2000, I would argue that the last twenty years should be given greater weight as this is when the Fed has really been active in driving the boom bust cycles. Also, in those cases where the indicator worked, one would have taken cash out just before a significant 30-40% fall; while in the 3 cases over the last 60 years when it didn't work one would have missed a 10-20% rally.

**Experience of 1974 and 2008**

**Charts –P/E 10**


**Charts –S&P 500 Forward P/E–Yardini research**


To ensure we are not late in cutting exposure, we will overlay the technical metric with the ECRI Leading indicator, which has had some success at highlighting periods of economic slowdown. Right now, it would indicate we are potentially falling rapidly into a recession.



If we do see this economic weakness come through and the FED acts irrationally and tightens into it, this will put further pressure on risk assets. Should this scenario play out, the good news is that we would likely experience a dramatic, but short fall off. As opposed to a lengthy bear market like 2000-2003.

The asset classes that would do very well here will be:

- Bonds will rally as we move through the decline, and we are as a result adding to long duration sukuk in the Muti-Asset Fund, namely the SECO '44, which gives us a yield to maturity of 5.1%.

- The Disruptive technology strategy would likely weaken in alignment with the market, but would rally sharply off the lows, as the Fed pivots. These stocks will perform best in a low growth, low-rate environment.

- Gold should do ok but will be volatile. Initially gold will get sold off as investors seek liquidity (just like 2008) and add to USD holdings, but will come back strongly with the Fed pivot. Also, gold should do very well as the Fed pauses and the ECB starts to tighten.

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