

INDEX House View

For investors who have passed through decades of economic cycles, current market moves continue to be defiant towards traditional economic theory. These are indeed strange times. Fears of an inflation spike seem to be reducing, as we enter the second half of March. The rise in US bond yields seem also to be stumbling somewhat, which does not necessarily mean there isn't further upside to it – looking at the 34-year long trend in US rates, the 10-year t-bill yield can go up to 2.6% from the current 1.63%, reaching its technical upper limit. US inflation is picking up slightly, now reading 1.7%. This metric too is within its long-term trend band, meaning that it is perfectly normal for inflation to rise after a period of stagnant consumer demand – a point that is anyway debatable, since high-street demand has been more than matched by online demand during 2020, making the argument that inflation remained constant rather than decrease during the lockdown period in developed markets.

In simpler words, macroeconomic trends are telling us that major metrics are simply normal. Markets might be on their way to recognized that, as a sharp correction in growth stocks – see tech and semiconductors – and other stretched industries happened in the past three weeks. We interpret this as a pause in investors' greed rather than a change in risk attitude. With the excuse of rising yields, a good number of participants (institutional, we think) might have thought that 1.63% on US 10-year t-bill is a great risk-free parking spot, worthy of exiting overvalued stocks and wait for some good equity opportunities – 1.63% nominal rate minus 1.7% inflation is a close-to-zero real rate of remuneration of your capital.

At the same time, good opportunities have recently emerged in our list of target stocks. Late in 2020 we decided to renew our market approach by placing 50% in stable, quality, solid and unique businesses, and 50% in growth stocks with solid tech, a pathway to commercialization, strong market positioning or absolute reign over operating costs. This strategic approach provides a strong basis of quality from companies that rarely see a downward adjustment of more than 30%, which essentially embodies the concept of margin of safety. The remaining portion of the strategy provides concentration on stocks with a high probability of future superior earnings growth and returns, as they contribute to the building of new industries or to the structural change of existing ones. This approach has already produced meaningful results so far into Q1, and we believe it is a good adaptation of our long-term Value Investing style to current market conditions.

This approach is also supported by the change in administration in the US, apparently towards a more professionalized approach towards global alliances and rivalries. Recently, tech bans were lifted against Chinese stocks, with a consequent market value jump – see Xiaomi. In wider terms, positive developments on the global pandemic situation are also impacting positively a general economic recovery, or at least encouraging the beginning of it. China itself is living better economic times as the pandemic gets reined in by way of vaccines – industrial production better than the past two years, investments in real estate going through the roof (equaling 2010 levels, post GFC), GDP on its way up to normalization, trade balance perfectly normalized, international transactions with the rest of the world picked up considerably (equaling pre-GFC levels in 2008). Europe is still fighting with gross political mistakes in distributing vaccines, in fact delaying economic recovery, but markets remain unperturbed by this last-minute changes – the most inclusive equity indexes, such as BE500, have reached pre-Covid 19 levels already. Last, Japan is passing through some volatile times towards economic normalization, but its weight in global GDP is only about 4%.

In this environment of general positive expectations on global economic recovery, investors do not seem to have changed their risk stance from March 2020. Yes, certain sectors cooled down, but more probably for rotational or profit-taking reasons rather than for a generalized risk-off sentiment. Many hedge fund managers have commented that it is impossible to bet against the market, specifically going short on entire indexes, geographies or industries – but it can work on single names. We tend to concur with this assessment, since we find no imminent risks that could diminish the excess of capital around, invert expectations on nascent industries or on changes to existing ones, or change the major monetary authorities' approach to the overlevered world they themselves created. It is in these conditions that we find opportunities in the equity world, as fixed income is very far from giving an adequate remuneration of capital.

For further details, please contact:

INDEX & Cie Limited

Index Tower, 20th Floor, # 2001

Dubai International Financial Center

PO Box 507069, Dubai, UAE

www.indexcie.com

Tommaso Leodari

Chief Investment Officer

Email: tl@indexcie.com

Disclaimer

The information herein contained, including any opinions and any terms and conditions presented (the "Information") has been prepared and distributed by INDEX & Cie Ltd. (the "Asset Manager"), and is directed at, and related financial products or services are only available to wholesale clients (non-retail customers) who qualify as either Professional Clients (as defined in DFSA's Rulebook, Glossary Module ("GLO") or Market Counterparties (cf. GLO) under the Rules (cf. GLO) enacted by the Dubai Financial Services Authority ("DFSA"). This document is being furnished to the intended recipient solely for information purposes and no other Person (cf. GLO) shall act upon the Information. Any investment carries its own risks; the investor must be aware of the risks posed by an investment (cf. GLO) and is fully responsible for the risks incurred. The Information is not and cannot be understood as impartial investment research. The Asset Manager does not guarantee the accuracy or completeness of the information and the opinions expressed herein are the Asset Manager's opinions at the moment they are conveyed only and are subject to change without prior notice. The Asset Manager is not under any obligation to update or keep current the Information and the opinions expressed herein. Neither the Asset Manager nor any of its officers directly responsible for the Information (or a close relative - cf. GLO - of the latter) have a financial interest or material interest that relates to any on the investments herein recommended or suggested, nor the Asset Manager either, as far as the Asset Manager is aware of, any Asset Managers associate (cf. GLO) owns (unless stated otherwise elsewhere in this document) 1% or more of the total issued share capital of any of the Issuers (cf. GLO) mentioned herein. The Asset Manager does not act as a corporate broker to any of the Issuers (cf. GLO), although one of the Asset Manager's associates may act or have acted as such. The Asset Manager has not undertaken any corporate business with or for any of the Issuers over the past 12 months, nor has in the pipeline any future relevant corporate finance business initiative involving the latter, nor is a market maker (cf. GLO) in any of the investment recommended. None of the Issuers herein mentioned has a material shareholding in the Asset Manager. This document cannot be reproduced, in whole or in part, in any form or by any means, without the Asset Managers specific authorization and any distribution of the information on behalf of the Asset Manager is strictly prohibited. Neither this document nor any copy hereof may be sent or taken or transmitted into or distribute, directly or indirectly, in any jurisdiction other than the Dubai International Financial Center. Any failure to comply with this restriction may constitute a violation of the laws of the jurisdiction where the document is being redistributed. This document does not constitute or form part of, and should not be construed as any offer or sale or subscription of or solicitation of or invitation to make any offer to purchase or subscribe for any financial products or services and neither this document nor any part of it shall form the basis of or be relied on in connection with or act as an inducement to enter into any contract or commitment whatsoever. The Asset Manager does not accept any kind of liability for losses or damages which may arise from the use of this document or its contents, nor for the unlawful reproduction and/or redistribution of the same. The Asset Manager is duly licensed and Regulated by the DFSA.