REYL
OVERSEAS

STRATEGY OUTLOOK

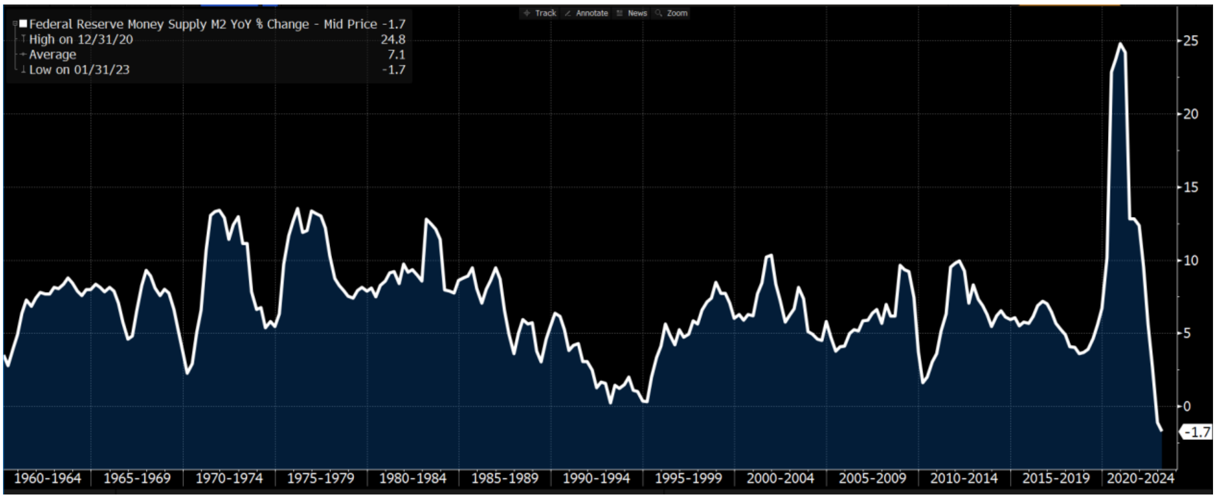
March 2023

Key takeaways-

- Just like February in Zurich the economic outlook remains foggy and grey…
- But opportunities exist, and we expect a far better year than 2022.

Here in Zurich, over the winter months, we get this perma-fog/cloud sitting above the lake. Drive one hour and climb a few hundred metres and vitamin D levels can be recouped so it really is a very minor complaint about living here. However, the analogy perhaps helps explain the economic outlook. The year began with the market pricing in a recession, interest rate cuts and asset markets duly rebounded. Then in February we saw a raft of data dramatically about turn and question the market pricing of even a pivot and indeed whether yet more hikes from the Federal Reserve would be forthcoming. Ultimately **the market has been left thoroughly confused – inflation or deflation, growth or recession, jobs, or unemployment.**

We don’t think we can downplay the lasting impact of what the global economy has gone through over the last 24 months because of covid but, far more importantly, the economic and social policies that were brought to bear. For **example, the amount of money injected into the veins of the US economy was truly unprecedented** as the graph of money supply (below) highlights. Then a new cold war was reignited under the guise of Ukraine, as inflation kicked a lot higher and global central banks (and investors), arguably, were caught napping.



Any interest rate hikes today will take approximately two quarters i.e., roughly till October 2023 onwards to feed into the system. We have had 4.5% of hikes already since a year ago. There is therefore a diverse range of competing drivers fighting for influence. Boil these down and it’s tough to have any real certainty in your view. **But then to what extent should we try to second guess inflation or the Fed.**

Irrespective we are a lot more confident holding to and trading around our structural or longer-term views. One example of this is the energy transition. Google Wikipedia for the Industrial Revolution and it’s dated from 1760 to about 1820/1840. The calls to stop using oil tomorrow are, at best and politely, not realistic and so we feel very confident looking to both new and old technologies within this theme for investment opportunities.

Another longer-term view is de-dollarisation. China has built in Africa 100 seaports, 1000 bridges, 10,000km of railways, 100,000km of highways and 200,000km of optical cable**. Dollar hegemony is under threat**, the BRICS nations are moving away from the Greenback and US Treasuries to gold and commodity backed currencies. Yet the timing is probably a lot shorter than the industrial revolution but it’s clearly in progress.

The Ohio train crash perhaps highlights some issues. Domestic US infrastructure spending is hugely needed, and the handling of the environmental and social damage missing as we understand it. The President flew out to hand, yet more cash, over to the pawn in this cold war- Ukraine while Trump flies to Ohio and hands out food. An easy political win. Yet Trump's Achilles is he's either loved or hated with little middle ground.

The 2024 election circus has started. We are sure the current Administration is very mindful of where we are in the business cycle running into the election and subsequent pressure will be being exerted on the Fed to not make the economy a talking point. Nikki Haley has thrown her hat into the ring and made things interesting as we don't think it's in anyone's interest to have another Trump vs Biden mud slinging contest on who is the least senile. But we suppose it's a bit like dating or interviewing. You never really know what you get at the end of the day, and it will be the same with Haley or DeSantis or possibly John Kennedy Jnr.

Walmart, the world's largest retailer, released earnings which disappointed and saw the second straight annual decline in profits. Their outlook points to a slow rebound but robust grocery sales. Their CFO said the following in an interview –

"We feel good about how the core business is operating, but we're **cautious** with the macroeconomic outlook" and "There's a lot of **unpredictability** around what's happening, what will be the effect of Fed tightening on the consumer balance sheet, what is the effect of the declining savings rate ".

Home Depot, the home improvement retailer, also saw profits decline as spending slowed and wages increased. **Nestle**, the world's largest food company also voiced concern about continuing increases in the price of food. The firm increased their prices last year by 8.2%.

The fiscal picture in the US remains a big concern. If you believe the stats then US unemployment is running at its lowest level since 1969, the latest jobs report was a "blockbuster" and wage growth is running at 6.1% yoy in January. Yet US January tax receipts are down over 7% yoy. Q1 this year the US Treasury is set to borrow $932bn or 60% higher than expectations from the previous quarter. If the Fed keep hiking, they will see yet weaker tax receipts, higher deficits and borrowing and perhaps US Treasury market dysfunction which will send the USD higher and stocks south. Not what any politician wants. The USD is the release valve, and this must be pushed weaker. The good news is that that's good for precious metals, commodities, Bitcoin, and equities.

The issue is that if Yellen can get the USD weaker there is $4.82 trillion sitting in US money markets and that's **bullish for assets** but also, potentially, inflation. Another area of potential bullishness is global liquidity and in particular Japanese yen intervention. It was interesting that former Fed official Kathleen Tyson took to Twitter to state "Stealth intervention to support the yen fits with my suggestion around mid-

October of New York Fed support for BoJ in exchange for two small islands now being fitted with US missiles for WW3. And BoJ reserves have been growing since as BoJ buys more USTs". Follow the money.

For markets the economic outlook remains uncertain. Geopolitics and the warmongering are ongoing concerns and recent statements from Malaysia and Singapore perhaps highlight there is a lot more going on than being publicly discussed. There seems to be growing political support in Washington for anti-Chinese legislation and regulation. Perhaps the election fever can't come quickly enough to re-direct focus! Additionally, the US fiscal situation is a real bind, and we expect dollar weakness into the rest of the year and hence supported markets. Broadly we remain defensive with an underweight in equity and cash on the side-line. Ultimately, we believe stocks are bottoming and are looking for opportunities to get bullish. We did reduce our bond exposure last month on ongoing fiscal concerns which we have discussed. Going forward we have and are adding niche investments which fit our strategic themes, and which don't require as much of a binary bet on many of the issues discussed.

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