Incrementum All Seasons Fund

– in pursuit of real returns –

2020 / 04

April 2020

Seasonal Reflections

What goes up…

<u>Quote(s) / Chart(s) of the Month:</u>

"The investor who permits himself to be stampeded or unduly worried about unjustified market declines in his holdings is perversely transforming his basic advantage into a basic disadvantage." (Benjamin Graham; Source: What Benjamin Graham Would Tell You To Do Now by WSJ, March 10, 2020)

"The problem is, the pandemic of fear is spreading much faster than the actual virus. China had 80,796 cases as of yesterday, with a population of 1.4 billion. South Korea had 7,869 cases, with a population of 51 million. They're making progress, apparently, in China and South Korea in containing the virus, and even in the epicenter of Hubei province they're talking about slowly resuming transportation. I don't know what purpose it serves when [German Chancellor] Angela Merkel scares the living daylights out of people. [Merkel has warned that 70% of Germany's population could contract coronavirus.] It didn't even spread to 70% of the Chinese. People aren't focusing on the fact that 80% who get infected are likely to suffer only mild symptoms, and that may be understated; that the most vulnerable are older people. Italy has everyone spooked: It has a highly geriatric profile, and we know that older people are more susceptible to the virus. Put this into perspective: Nearly 1.25 million people die in road crashes each year globally, on average, 3,287 a day. An additional 20 million to 50 million are injured or disabled." (Source: Why the Bear Won't Depart Until Midyear, Barron's Interview with Ed Yardeni, March 12, 2020)

"We are experiencing the end game of the great debt super cycle. As the private sector has become increasingly over-levered, the baton is being passed to the public sector where resources are so strained that the printing press has become the last resort." (Source: The Faustian Bargain by Scott Minerd, Global CIO, Guggenheim Investment, March 27, 2020)

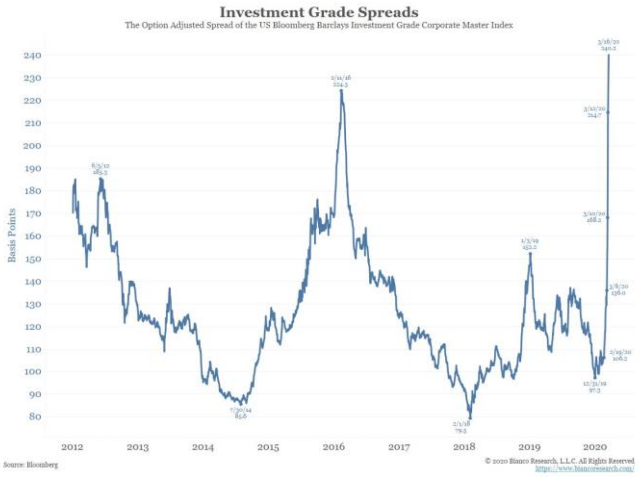
"Question. - Tell me last time stocks & Treasuries sold off as much as today? - Never!
The S&P 500 is down 16% in the last 7 days while 10-year yields more than doubled! Some risk parity funds are already down 40+% in a month!" (Source: Otavio Costa, @TaviCosta, on Twitter, March 19)

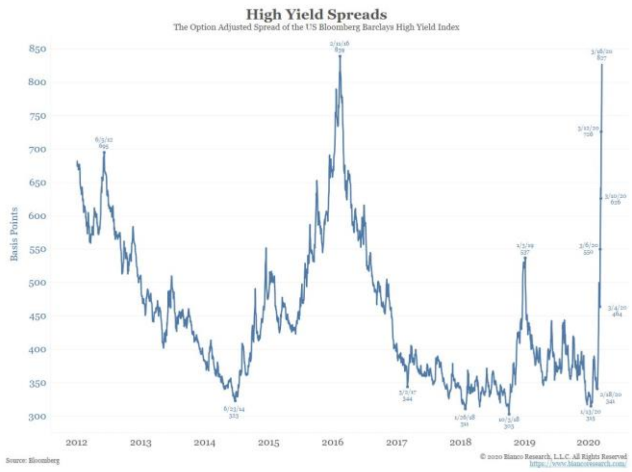
"The Federal Reserve will let Wall Street banks take on more leverage so they can absorb some of the stress the central bank has seen in Treasury markets, the agency announced Wednesday." (Tweet by Jonathan Ferro, referring to a Bloomberg article)
"That's what we need, more leverage, more debt and more intervention.
How about: More sense?" (Reply Tweet by Sven Henrich @Northman Trader, April 1, 2020)

"In a normal economic environment, OPEC discord is enough to crash oil prices. An OPEC price war occurring in the midst of a global demand shock (i.e. the Coronavirus outbreak) is completely unprecedented. We are in unchartered territory. Thus, without a reversal of stated OPEC policy, oil prices are headed back to their 2016 lows ($26 Brent) and likely lower. ***Logic dictates we downgrade oil from neutral to bearish. This could be a short-term downgrade. We expect gamesmanship is at work. Whether we are discussing U.S. shale, Saudi Arabia, or Russia, sub-$40 oil works for no one."*** (Source: Energy Armageddon by Ned Davis Research on Realvision, March 9, 2020)

Headline of the Month: ***"Congress Allocates $2 Trillion To Bail Out Struggling Bailout Industry"*** (Source: The Onion, as quoted in Almost Daily Grants, March 17, 2020)

Charts of the Month:





Source: Jim Bianco on Twitter, headlined "Bad, very bad!"

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Dear Reader,

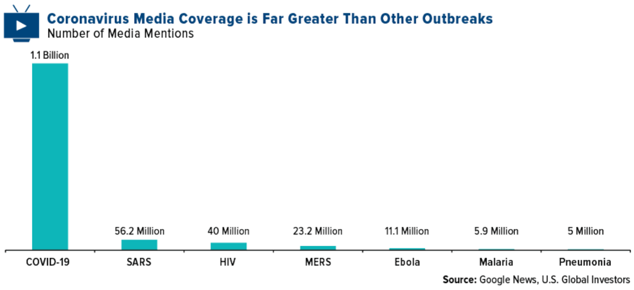
I opened my last Seasonal Reflections from March 9 with a remark about what a wild ride February had been in financial markets. – Little did I know…

Source: pexels.com

March 2020 will end up in the investing history books as important reminder of what a "wild ride" actually is…. – In fact, during 1Q 2020, global equity markets went from buying-the-(tiniest)-dip market mentality to mindless selling in the span of six weeks, which has provided a whole new definition to the risks of investing and the short-term pain it can dish out.

For years I had written in these pages about the awful combination of lacklustre world economic growth, coupled with major structural issues, i.e. ageing societies, monetary policy increasingly ineffective, and economies toiling under too much debt, to name just a few. In this cocktail the spread of SARS-CoV-2, commonly referred to as Coronavirus (CoV), proved a splitting headache inducing ingredient. And for the record, I also underestimated the CoV induced demand shock and market effect.

But don't worry, I am not about to turn into another armchair epidemiologist who seem to be rather abundant in numbers these days. Like many others, I have read much of what has been said by the experts, but this doesn't make me qualified to opine on the subject with any authority.



Source: U.S. Global Investors, March 16, 2020

Besides, I reckon you will all be growing tired about this anyway. After all, whatever your favourite media channel, CoV and the measures to contain its spread dominates the news more than any other viral outbreak we have seen in recent years, some of which appear to have been more lethal in their effect.

Schaan Industry, Ivoclar Vivadent Staff Parking Lot, Mar20, 8am (HGS pic)

Here in FL, similar to the rest of the world, we are also in a state of voluntary lock-down, with schools, entertainment venues and all shops except groceries and pharmacies closed. With most people home-officing, it is truly eerie out there.

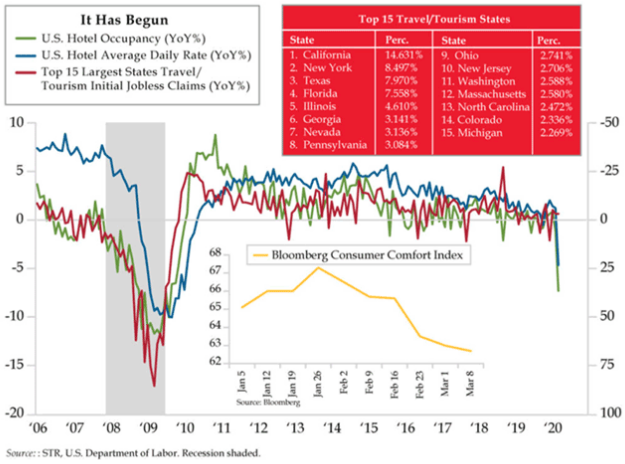
Pedestrian Area, Centre of Vaduz, Sat, Mar28, 11am (HGS pic)

Being currently in the fourth week of essentially shutting down the economy, however, I cannot help wondering whether our political leaders and bureaucrats are not overdoing it with these heavy-handed, broad-sweeping top-down measures. And here my concerns reach beyond the short-term effectiveness of the steps taken to contain the virus, which may well be setting a bad precedent for future attempts to curtail our freedom, as I had briefly commented about in this [Tweet](#) from April 4.

But the focus of this letter is on investment implications, and with this in mind I believe investors are still underestimating the economic damage this partial closure of our economies creates. With Q1 over and CoV containment measures applied around the globe, the media are saturated with predictions about the depth of the resulting recession. The gulfing spreads of these forecasts however highlight the extreme degree of uncertainty they are made under. – Why do I believe this?

Because this is NOT your garden variety recession, which is caused by monetary and large company belt tightening, and which follows standard patterns that analysts know how to track. This lock-down hits consumption and the labour-intensive service sector the most. The resulting shock to employment is clearly evidenced by the chart on the right.

US Jobless Claims, last 50+ years, Source: Refinitiv



Source: Danielle DiMartino Booth, via John Mauldin's "[Coronavirus Helicopter Money](#)", March 13, 2020

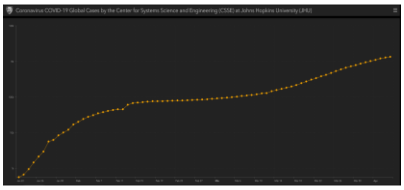
I guess you all will know how much you have spent in hotels / restaurants these past four weeks (let me guess, zero?), and thus the chart on the left only marks the beginning. This should not be a surprise considering that major conferences / events were cancelled / postponed amid CoV fears, e.g. Mobile World Congress Barcelona, ITB Berlin, Geneva International Motorshow, Tokyo Olympics, etc. Meanwhile, business (and leisure) travel has practically come to a standstill, with major airlines reporting 80 to 90% of flights being cancelled.

As the photo on the bottom right of the previous page suggests, retail business has been knocked-out flat, and from my own anecdotal evidence here handymen have also stopped most of their work projects. Tourism, which employs about a tenth of the global workforce, has been almost completely shut down. Personally, I had to cancel a trip to Tirol in March, my planned Asia business trip after Easter, as well as a visit to Hamburg in May so far, and I guess many readers will have made similar decisions.

Our girls have been home for more than two weeks already, and it looks like the family will be reunited for about at least another month. This is great, because with both of them grown up already, we don't usually spend that much time together. Thus, my wife and I regard this as rather fortunate circumstances. However, there are many families with small kids, who in this part of the world have been forced to stay mostly indoors, despite of the magnificent spring weather. I can easily imagine the stress this can cause for parents who try to juggle the duty of home-office, home-schooling (as most schools seem ill-prepared for remote teaching, while the students will be less attentive compared to sitting in class), managing the household and keeping the kids busy and entertained.

And what about singles? – Man is a social animal, but with current policies, both young and old will be bound to become lonely and possibly depressed. And phone calls or video conferencing are a poor substitute for actual get-togethers. Also in this regard, the current recession is rather different from conventional economic slowdowns.

Of course, there are still hopes that things will return to normal, as the so-called coronavirus curve, which measures how rapidly the disease is spreading, is flattening. But at this juncture, I don't foresee the world resuming business as usual before the end of 2Q at the very earliest.



Johns Hopkins University (log chart)

After all, it will likely still take considerable time to develop an efficient vaccine. Thus any exit strategies from the current lock-down regimes will mean a slow and potentially phased return to work, while continuing with restrictions on travelling and entertainment like sports games and music festivals. As an example dear to my heart the German Bundesliga will resume its delayed season in May, but all matches will be in crowdfree arenas.

Source: Sportbuzzer.de

The Kicker reported discussions by the DFL, which I guess some may say in typcial German fashion intends to admit only 239 people per match: These include both teams, coaching, support and medical staff, TV crews, as well as 4 ball boys (no kidding!), of which 113 people will be on the stands, 30 of which will be journalists… – Even die-hard fans may prefer to watch this from their couches instead…

Sorry for digressing… – Even if we assume a slow and phased resumption of "normal" working life, there will of course also always be the risk that restrictions need to be reimposed if there are further outbreaks before a vaccine is available. That promises to leave rather deep scars in the economic tissue.

Despite of the uncertainty involved in making reasonably accurate predictions under these circumstances, we are likely heading for one of the worst recessions ever. And for all the differences pointed out above, a meaningful loss of income and wealth is one issue that this recession has in common with its predecessors. Having said that, never before in my lifetime has been done more to try and counter this.

Source: Hedgeye

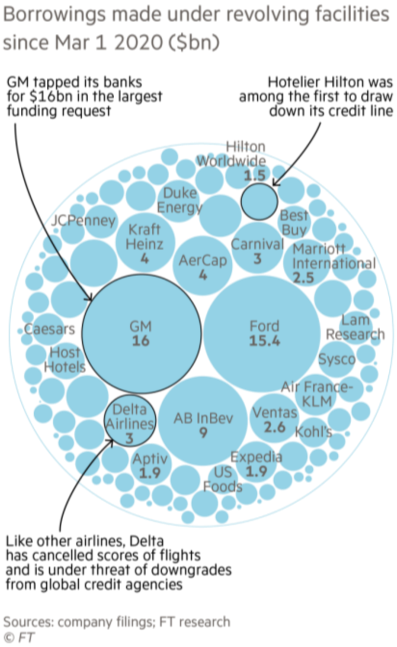
"You never want a serious crisis to go to waste. And what I mean by that [is] it's an opportunity to do things that you think you could not before." Though attributed to Rahm Israel Emanuel, former White House Chief of Staff to President Barak Obama, this has long been something any politician has known and understood, and our current leaders are certainly no different.

The US alone has so far agreed on a 2 trillion USD stimulus package, which consisted of billions of dollars of aid for large industries like airlines, but also smaller businesses. It also contained the first case of helicopter money, as USD 1,200 checques will be mailed to taxpayers earning less than USD 75k in annual income (plus USD 500 per child). The size of that program already dwarfs the combined deficit in 2008/09.

Source: Hedgeye

Similar stimulus packages have been wrapped up across Europe and beyond, and such fiscal support can easily amount to 10% of GDP. Given already strained government finances they can only be funded by central banks resuming their large-scale "asset" purchase programs, aka Quantitative Easing (QE), i.e. by creating currency out of thin air to use it to buy their government's debt obligations at above / below market prices / yields.

At the time of writing this, the battle for more support is raging among eurozone members, as countries that are hit the hardest by the CoV spread, most notably Italy, backed by France and other Southern countries, are pressing for the joint issuance of debt, which the Northern states have been refusing to underwrite so far. Using other tools like the European Stability Mechanism (ESM), which was set up in response to the 2011 eurozone crisis, is not seen as far-reaching enough. Quite frankly, the initiatives and tools available are plentiful, but in the spirit of never letting a good crisis go to waste this may well present an important milestone for the monetary, fiscal, and thus political future of Europe.

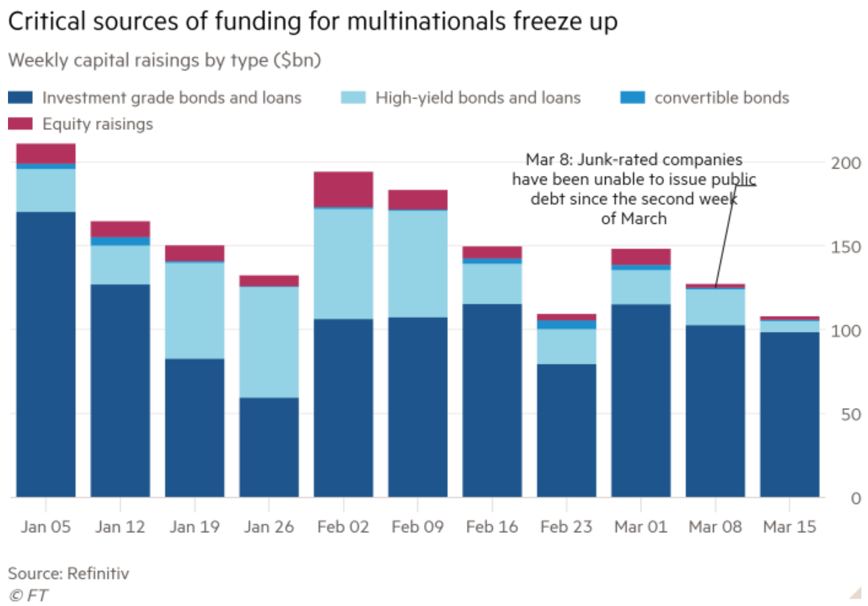


Source: [Financial Times](), March 25

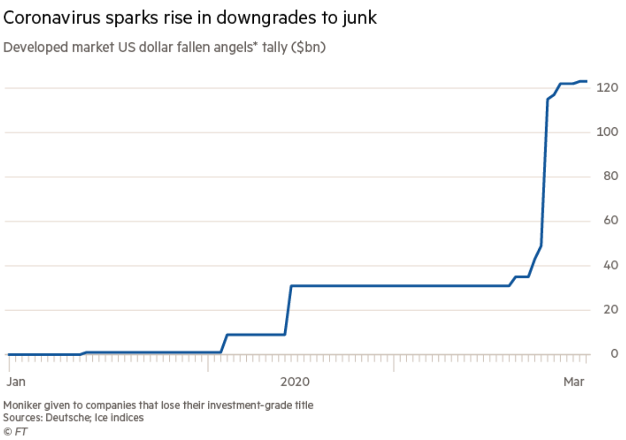
The speed and size with which companies have been drawing down their revolving credit facilities in March is shown above and reminiscent of the Great Financial Crisis.

But trouble in credit land is spreading far beyond the public sector, where trusted public servants have only the best interest of their citizens on their mind (cough, cough…)

While equity markets have captured the headlines in March, I guess the blow-out in corporate credit spreads, which is highlighted in the "Charts of the Month" on page 2, may well have caused a lot more terror among private and public bankers. Rising funding stress is also evident from the chart below.



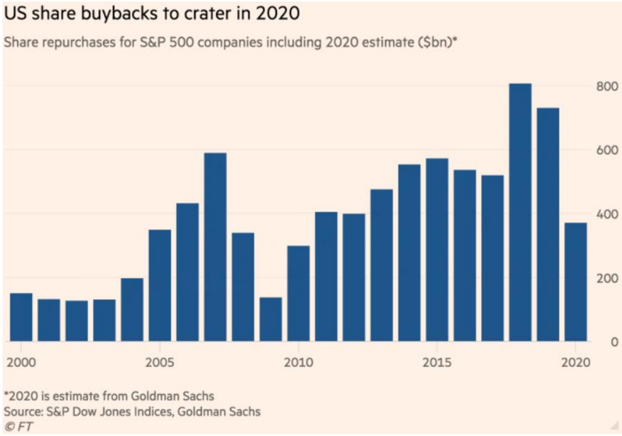
Source: [Financial Times](), March 25



Source: [Financial Times](), April 7, 2020

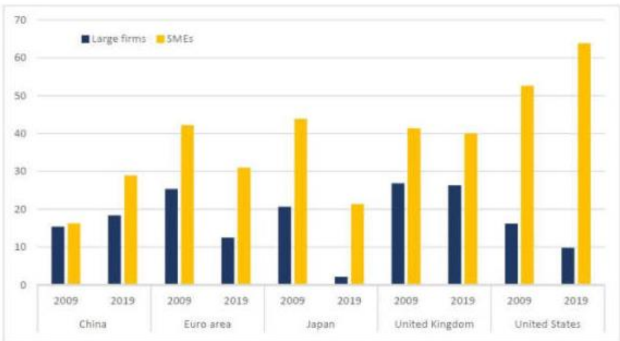
Such a run on short-term borrowing facilities underscores the financial stress many corporates are under. This is also evident when considering that according to the FT a record USD 90bn in corporate debt was downgraded to junk bond status in March. That number according to Bank of America could reach USD 200bn this year, which seems a small amount compared to the numbers mentioned earlier but has to be seen in relation to a total junk bond market size of an estimated USD 1.2 trillion.

Of course, this mainly represents the stress felt by large-cap listed companies with comparatively easy access to capital markets, whose management has been busy in recent years to ~~enrich themselves~~ increase shareholder value by raising debt in order to buy back shares. Although this has also been a European phenomenon, the US buyback bonanza has been clearly unprecedented. But many of the worst offenders are now lobbying their governments to provide financial assistance, aka bailouts.



Source: [Financial Times](), April 7, 2020

If you now think that perhaps small and mid-sized enterprises (SME) have been more prudent in their behaviour, you have not learnt anything (yet) about the lure of cheap money. I'll refer again to a recent article in the Financial Times, which quotes Bank of New York Mellon's Daniel Tenengauzer with respect to the accompanying chart from the recent IMF Global Financial Stability report, which depicts the percentage of debt held by businesses with Ebit-to-interest ratios below 1:



Source: [Financial Times](), *March 2, 2020*

"While large firms in the US seem to be quite shielded, SMEs could be quite vulnerable in the event of sudden stop in economic activity. These SMEs are primarily suppliers to larger firms, which may well have a meaningful trickle up effect to large companies' capacity."

Quite honestly, I was just wondering why I did not make this my Chart of the Month…

I am sorry, but for the uninitiated EBIT stands for Earnings Before Interest and Taxes. An EBIT-To-Interest ratio below 1 means that these companies generate insufficient cash to service the interest on their debt (assuming they are actually paying taxes). In 2019, large firms outside of China seem indeed better positioned in this regard, but the situation for SMEs seems particularly dire, with two-thirds of all loans in the US owed by small and medium enterprises that feature an EBIT-To-Interest ratio below 1. This is especially worrying because the years of comparison used: 2009 was already the year after the crisis, when earnings were at their most depressed levels, while 2019 was the last year of a decade-long economic expansion with record high earnings at least among the large companies.

I guess you are seeing the dilemma: Extremely elevated debt levels at record low rates meet the potentially worst recession in nearly a century. No wonder one begins to lose track of the alphabet soup of debt buying and stimulus programs. – Poor taxpayer!

By the latest estimates Germany's economy is expected to shrink by 10% during the second quarter, while France's GDP has shrunk 6% already during the first quarter. All the fiscal stimulus and tax relieve in the world will not help as much as hoped for, if people are not allowed to go out and spend, and businesses need to shut down or suffer from breakdowns in global supply chains. And while this may seem like an advanced economies problem, the situation is similar in the developing world, where fiscal room to manoeuvre is greatly reduced. Thus, China's GDP growth during 1Q is expected to fall by 10%, and full year growth come in at 2% only. And: *"In 2007, 40 emerging market and middle-income countries had a combined central government fiscal surplus equal to 0.3 per cent of gross domestic product, according to the IMF. Last year, they posted a fiscal deficit of 4.9 per cent of GDP."* (FT, March 17, 2020)

Ok, I guess you'll get the picture. My firm belief is that the CoV spread is a black swan type of event, which meets a world that is not quite prepared. At this point, experts expect a sharp recession during 1H 2020, but the base case that financial markets also still seem to price in is a V-shaped recovery during 2H 2020. Of course, there will be a recovery. But no one knows how sharp and thus painful the initial economic contraction will be, and whether all the money thrown at this by the authorities will actually be able to avoid a systemic collapse without creating runaway inflation at the other side.

So, what about financial markets? – How did they fare?

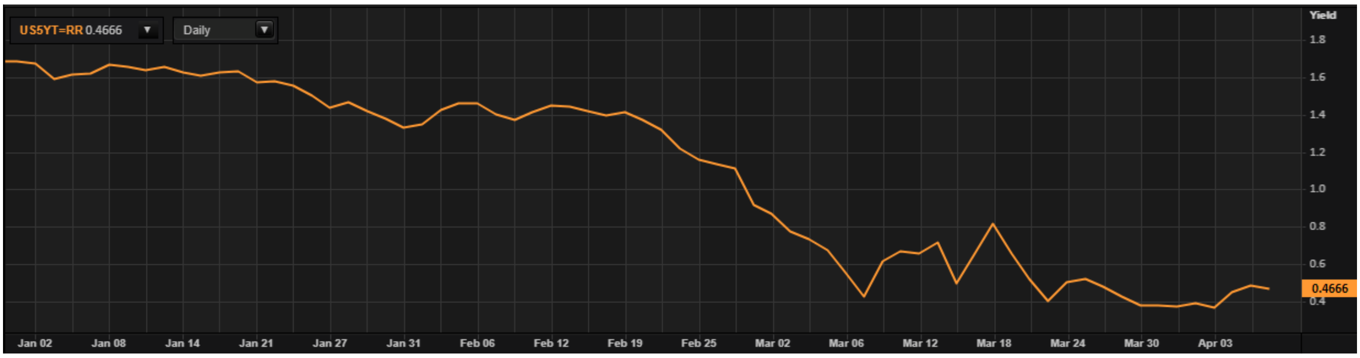
Let me give you a quick overview on quarterly developments below:

FTSE Global:	-15.6%	EUR/USD:	-1.6%	Brent Oil Future:	-65.5%
Euro Stoxx 600:	-22.6%	GBP/USD:	-6.3%	Copper Future:	-20.9%
S&P500:	-20.0%	USD/JPY:	-0.1%	Gold (XAU):	+ 3.6%
Nikkei 225:	-20.0%	USD/CNY:	+1.7%	Silver (XAG):	-21.6%
China CSI 300:	-10.0%	EUR/CHF:	-2.3%	Platinum (XPT) :	-24.8%

Equity markets (left column) have generally registered double-digit losses, with Europe faring the worst and China holding up relatively better. The worst decline happened in the span of five weeks between February 18/19 and March 23 and reached drawdowns of almost 40% (Euro Stoxx 600). Major foreign exchange pairs were relatively steady, except GBP which saw a more than 6% decline against the USD. Larger losses were also registered among commodity currencies like CAD, AUD and NOK, as well as Emerging Market currencies (e.g. BRL -30%, MXN -25%, ZAR -28%, RUB -27%, IDR -17%). The worst casualty of the CoV spread and resulting economic freeze was the oil market which saw crude oil prices collapse by two thirds. Large losses were also registered in industrial metals like copper, but precious metals were mixed with gold proving its safe haven status, while silver and platinum, which also have many industrial uses, got hammered as well.

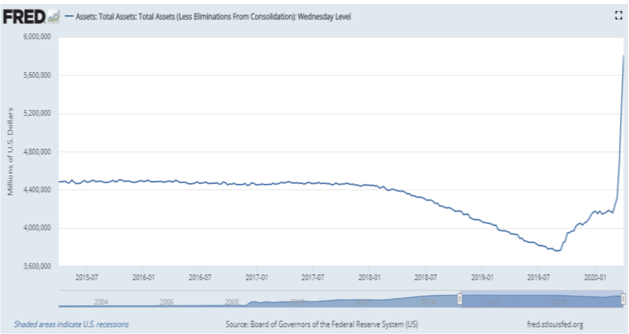
I will explain further below how this all has affected the Incrementum All Seasons Fund, but as you can guess it has not exactly been pretty.

What has worked this year for diversified portfolios is if they have had exposure to major advanced economies bonds, i.e. US treasury bonds, or German and other high “quality” European debt. I am putting quality in quotation marks, because it is still determined by respective yield levels, which continue to be extremely low. Case in point is the 5-year US treasury bond shown below:

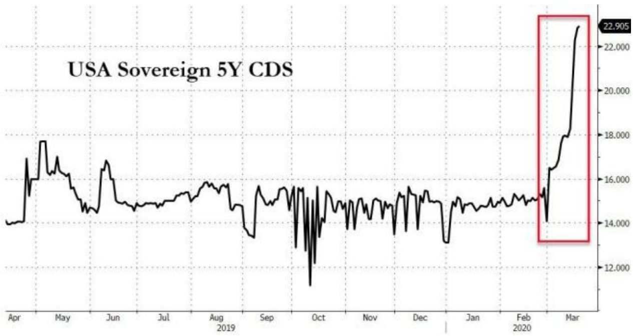


5-year US Treasury bond yield, year-to-date, Source: Refinitiv

But it is important to remember that these bond prices and yields are no longer market prices, but effectively manipulated by central bank buying, which has recently been boosted dramatically. As the graph below on the left shows, the Fed has increased its balance sheet via bond purchases by US 1.64 trillion USD between February 26 and April 1 alone, which is a staggering 40% in less than six weeks.



Source: [Federal Reserve Bank of St Louis]

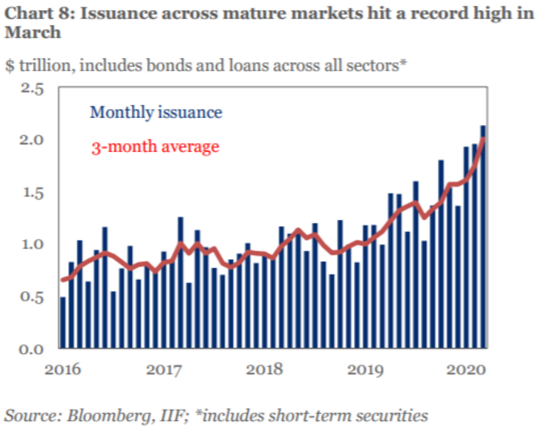


Source: [Twitter]

With so much price insensitive bond buying going on, it should not surprise that prices have risen (which they arguably did already in anticipation) resp. yields have fallen. But there is an obscure corner of the market that is still unaffected by this, namely the market for Credit Default Swaps (CDS), which are privately exchanged contracts that insure against the default of an underlying. And in the graph above on the right that indicates that insurance premiums to hedge against a default of 5-year US government bonds have recently gone up noticeably. Thus, whether investors really want to have that kind of “quality” in their investment portfolios for much longer remains to be seen. For your fund manager that is certainly no option and has not been for quite a while.

But apart from G7-type of government bonds there were obviously few places to hide over the past six weeks.

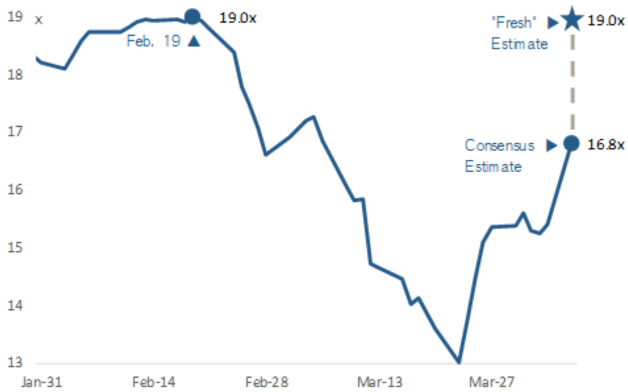
For those who may have thought that corporate or Emerging Market bonds offered any protection, think again. Despite of big central banks increasingly buying corporate bonds as well, spreads have exploded higher and thus yields over the respective government benchmarks have soared, leading prices to fall accordingly. Although similarly to equity markets there has been a bit of a relief rally of late, spreads still suggest extremely elevated stress levels and little investor appetite to load up the boat yet. And this should be no surprise considering the before described funding stress and the steadily rising bond issuance across all sectors.



Source of both charts: Bloomberg Opinion, Points of Return by John Authers, April 8, 2020

So, what about equity markets? – Is it time to rush in again and buy stocks? – Frankly, that is an argument we have intensely discussed here at Incrementum as well. The pro-argument is usually a basic supply-/demand observation: With central banks buying even more bonds and supplying so much liquidity, the only chance for investors to earn a decent return is in equities. The contra-argument: Valuations are still extremely stretched and thus equities may fall further before they offer an attractive entry level. It may not surprise readers that I am leaning more towards the second camp, though the degree of uncertainty is even higher than usual. If we look for example at valuations like the classic P/E ratio, it seems stocks have become cheaper amid the sharp fall in the numerator.

But this does not take into effect the expected impact on the denominator, as earnings are certainly going to fall sharply as well. The as usual thoughtful John Authers' has presented the accompanying chart of earnings estimates in today's "Points of Return", which show estimates that have been revised last week. Applying updated reduced earnings forecasts suggests that the P/E ratio for US equities is still near its February peak levels.



Source: Bloomberg Opinion, PoR, John Authers, April 8, 2020

But mostly, I am concerned about investors' sentiment. After a short period of panic, it seems that the same buy-the-dip mentality is getting hold of investors again. Personally, I have gone through quite a number of notable bear markets already and none of them was over after 6 weeks and with so little true despair being felt among investors. I certainly hope this time will be different, but I hesitate to bet on it yet.

Historical patterns show how these things tend to develop, and that significant falls are usually followed by sharp rebounds. This is succinctly depicted in the graph below on the left. But using the September 2008 blueprint (chart on the right) also suggests that the recovery seen so far is entirely in line with the pattern back then, and thus – also in light of the expected real economic pain this year promises to deliver – I believe investors should still treat carefully.

Source: Bloomberg; Points of Return, by John Authers, March 25, 2020

Points of Return, by John Authers, April 8, 2020

I expect a key question for investors going forward will also be how the political backdrop has changed. There are expectations that the current round of bailouts for Big Business may lead to a popular backlash against listed companies, who seem rather ill-prepared for the developing recession. Restricting or even prohibiting buybacks could turn out a real game changer for US equities, who benefited extraordinarily from the past buyback wave.

Figure 2: Corporations have been the only net buyer since the GFC

Source: breynoldsstrategy / Canaccord Genuity

Bloomberg reported that last year almost a third of companies in the S&P 500 paid out more in dividends and buybacks than they made in profits. Such companies may even feel it inappropriate to return to generous dividend pay-outs too quickly, as they will be keen or might be urged to keep more cash on hand to guard against future emergencies, putting at least a question mark behind the often-heard argument that one needs to buy equities for income.

Source: [Investing.com](https://www.investing.com)

Let's look at the FTSE Global 100 index above. Peak-to-trough it dropped 32%, and since the low on March 23, it has recovered approx. 50% of that decline. This is almost a text-book retracement, and it happened against a materially deteriorating economic backdrop. Investors seem to focus mainly on the flattening of the CoV curve, while disregarding that this was bought by essentially putting the economy in a self-induced coma. We are only now heading into 1Q earnings season, which I expect will surprise many with its sobering outcome.

Corporate boards who look for government support and bailout will use the CoV argument to do all sort of kitchen-sinking, and I expect an exceptionally poor set of results, with an exceptionally uncertain outlook / guidance for the further course of the year. Has this been priced into consensus analysts' estimates? – Obviously not!

Measure	Actual	F12 Est	Growth	Y+1 Est	Growth	Y+2 Est	Growth
1) Earnings Per Share	152.00	156.32	2.85%	177.83	13.76%	199.30	12.08%
2) EPS Positive	154.40	158.16	2.43%	178.56	12.90%	199.53	11.74%
3) Cash Flow Per Share	233.61	230.40	-1.37%	260.73	13.16%	283.92	8.90%
4) Dividends Per Share	60.58	64.96	7.24%	64.40	-0.87%	67.49	4.79%
5) Book Value Per Share	913.57	955.31	4.57%	1027.78	7.59%	1118.66	8.84%
6) Sales Per Share	1394.61	1404.48	0.71%	1473.17	4.89%	1560.81	5.95%
7) EBITDA Per Share	277.98	273.95	-1.45%	298.66	9.02%	325.04	8.83%
8) Long Term Growth	0.00	7.05	0.00%	0.00	0.00%	0.00	0.00%
9) Net Debt Per Share	505.73	545.30	7.82%	515.97	-5.38%	358.57	-30.51%
10) Enterprise Value Per Share	3040.80	3092.86	1.71%	3064.16	-0.93%	2898.50	-5.41%

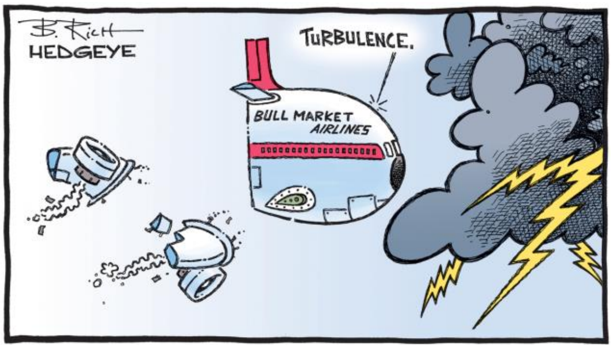
Valuation Measure	Actual	F12 Est	Y+1 Est	Y+2 Est
11) Price/EPS	17.50	17.01	14.95	13.34
12) Price/EPS Positive	17.22	16.82	14.89	13.33
13) Price/Cash Flow	11.38	11.54	10.20	9.37
14) Dividend Yield	2.28	2.44	2.42	2.54
15) Price/Book	2.91	2.78	2.59	2.38
16) Price/Sales	1.91	1.89	1.81	1.70
17) Price/EBITDA	9.57	9.71	8.90	8.18
18) EV/EBITDA	10.94	11.10	10.18	9.36
19) Net Debt/EBITDA	1.82	1.85	1.69	1.56

Source: S&P 500 Earnings Estimates, Bloomberg (April 8, 2020)

And even when we hope for a flattening CoV curve and the resulting drop in actual loss of human life, it will take a lot of time to get the economy back into full pre-crisis working mode. We can see already that Asian economies are struggling with this, as secondary or tertiary infection waves create partial resumptions of containment measures, including their negative impact on the economy. It is also important to bear in mind that different continents are in different phases. While Asia seems to have dealt with the worst impact already, containment measures in Europe are just showing the desired effect and will still last for a few more weeks, while the US is at an earlier stage still. With the tight interconnectedness of our world amid trade flows and supply chains, the effects of this will in my view be felt for at least another couple of months.

Thus, my base case is – unfortunately – that we have not yet seen the worst as investors still need to wake up to the actual economic damage this recession will cause. Hence, I do expect at least a test of the March lows, and possibly new lows over the course of the second quarter.

Am I too bearish? – Sure, that is possible! But having experienced such a poor start into this year with IASF's allocation to economically sensitive stocks, and looking at the trends unfolding and weighing on the real economy, as well as the impediments for the financial, corporate and household sector described above, I would rather prefer to err on the side of caution.



Source: [Hedgeye]

Yes, there is massive government intervention, but as with all non-market directed interventions, it remains to be seen how effective these can be. And I haven't even started on the question what all this will do to the -flation outlook (first de-, then in-?). But I will leave that for another day, as Easter is near and this may well be already stretching my esteemed readers' patience.

Now, let's look at how IASF has fared last month and so far this year. As usual…

Any investment views, analysis, assumptions and recommendations included in this letter are based upon current market conditions, reflect the opinion of the author, and do not necessarily correspond with the views of Incrementum AG as a whole. Seasonal Reflections are issued for information purposes only and must not be regarded as attempt to solicit an investment in individual securities or the Incrementum All Seasons Fund. Past performance is no guarantee of future results. All investments involve risk including the loss of principal.

IASF Month-over-month NAV change

March 2020 (27.2.-26.3.)

EUR-D	85.50	-11.39%
USD-D	87.13	-10.96%
CHF-D	84.30	-11.21%
EUR-P	84.21	-11.42%

For Charts, See Page

When I wrote my January Seasonal Reflections, contemplating the outlook for 2020, this was **NOT** what I had been expecting, namely a double-digit loss by March…

IASF Quarterly NAV change

1Q 2020 (31.12.-26.3.)

EUR-D	85.50	-18.17%
USD-D	87.13	-17.86%
CHF-D	84.30	-18.12%
EUR-P	84.21	-18.26%

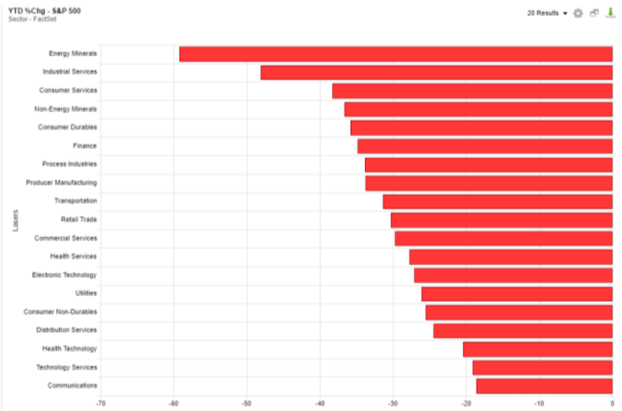
For Charts See Page

In fact, I had high hopes that the portfolio would prove relatively robust and perhaps even manage to deliver a positive performance during times of market stress. What I clearly had not envisaged was the impact the CoV pandemic and the resulting containment measures would have on IASF's real asset dominated portfolio holdings.

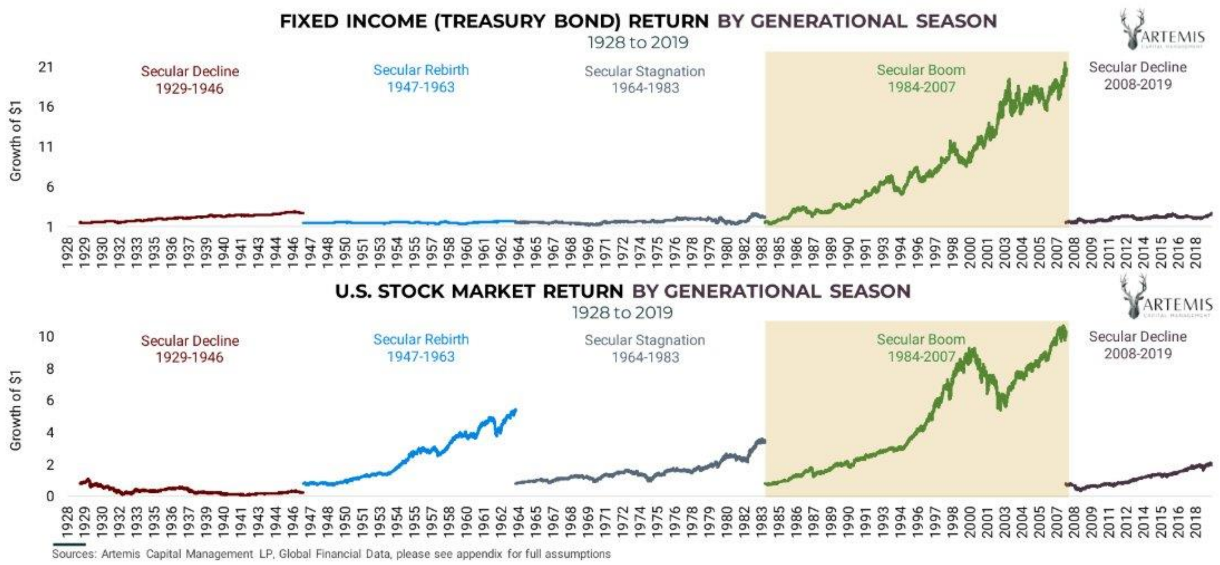
I am not going to self-castigate, but needless to say I am disappointed with the result so far this year. But as the opening quote on page 1 by the father of value investing suggests, I have always been a persistent investor, who does not *permit himself to be stampeded about unjustified market declines in his holdings*, though I guess it is only human that at times I find myself perhaps *unduly worried*. This in particular during market events where *"the 3 C's of successful long-term investing, which are Capital, Conviction and Courage"* (page 8 of Seasonal Reflections 2020 / 03) are required and an investment manager's mettle is tested. – And that test is still going on!

But ask yourself: How do we describe market trends? – "The bottom" / "The top" of the market is always the day before a long-term trend recovery / decline begins, i.e. they are only ever determined in hindsight. And for every "bottom" or "top" day there are hundreds of short-term trend changes, that may or may not turn out to be **THE BOTTOM** or **THE TOP**. Thus, I sell when things look expensive, even if in recent years they have tended to become more expensive (until this year, that is), and buy when they are cheap (even if sometimes they become cheaper still).

A good example is my exposure to gold and precious metals miners, which having been a drag for quite a few years have recently turned out to be significantly positive contributors to portfolio performance. And I reckon it will be similar with IASF's energy, other commodity and shipping exposure, which belong to the most dramatically punished sectors this year, though at this juncture I am the last to dispute that this is likely a 2H 2020 if not 2021 story.



Source: Risk Waits For No One by Factset



In terms of asset allocation, and referring to the graph on the previous page, it is also worth noting that *"91% of the price appreciation for the classic portfolio over 90 years came from just 22 years between 1984 and 2007. Large capital flows from boomers, falling interest rates (19% to 0) made this happen. Ask your advisor or pension the trillion-dollar question, is this repeatable?"* (Source for quote and graph: Artemis CM's Christopher Cole on Twitter) – The "*classic portfolio*" is a typical 60 / 40 (or equal-weighted) stocks and bonds portfolio, and the notion that the diversification effect between the two will continue to generate outsized absolute returns as we saw them over the past forty years is certainly questionable. After all, both bonds and equities enjoyed secular bull markets, with the former causing the latter. That is due to the fact that interest rates are the price for capital and are used to discount future cash flows. Lower interest rates do not only mean higher bond prices, but also a falling discount factor for expected equity earnings / cash flows / dividends, which in turn leads to rising share prices.

"Most of our consensus knowledge on investing is informed from four decades of unparalleled asset price appreciation and is not always true. The mantra of "buy on weakness" and the popularity of passive indexation would not have worked for most of the last 90 years. For example, if you bought on market declines consistently between 1929 and 1970, you would have gone bankrupt three times. A passive index realized a -86% peak-to-trough decline in the 1930s and two decades of lost performance. U.S. Treasury Bonds lost -25% unleveraged through the 1970s and -51% volatility-adjusted to Equities. … We often forget the last forty years were an extraordinary time to allocate capital, and if you just held risk and applied leverage to growth, you did exceptionally well. History has rarely been so kind to investors." (Source: The Allegory Of The Hawk And Serpent by Artemis Capital Management, Page 3)

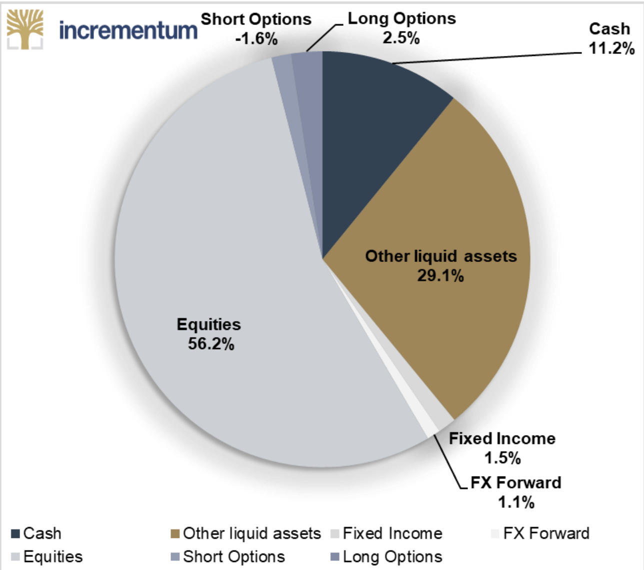
This is the reason why I have stopped allocating funds to government bonds, as they are artificially propped up by central banks, and in my own opinion will at best deliver positive nominal but negative real returns over the coming decade. And corporate bonds until recently offered similar prospects, though this may be changing again. What must be said, though, is that a not insignificant part of this year's negative IASF performance was due to the perceived risk-free liquidity. Investing liquidity into EUR alternatives like NOK (-16.5%), or into Silver (-20.4%) and Platinum (-30.3%) backed ETFs has raked up double-digit losses, which I had rather preferred to avoid. Thus, the NOK position contributed -1.24% loss year-to-date, the Wisdom Tree Silver ETF -0.59%, and the Wisdom Tree Platinum ETF -0.7%, for a combined -2.53%. This is an example of risk showing up in places where I had not expected it.

There are other examples for this, but as we all know this is hindsight, and hindsight always affords us the level of transparency that many investors think investment professionals possess as clairvoyance. This, unfortunately, I do not possess. What I can bring to the table, though, are analytical abilities, whether on the micro- or macro level, coupled with a wealth of experience in navigating the emotionally challenging aspects of market turbulence like we have witnessed this past month. Coupled with the necessary patience in the investing process this should yield decent results in the long-term.

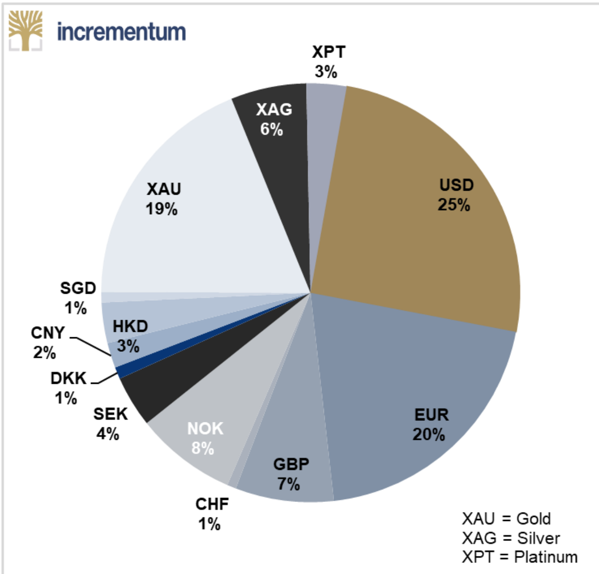
Well, let's look at portfolio positioning at the end of the quarter, and let me add some further comments here: IASF ended the month of March with approx. EUR 37m (USD 40.5 / CHF 39.1m) in assets, and there were neither in- nor outflows last month.

End of March allocations are as usual shown below. They show a slight increase in equity allocation to 56.2% (+0.7%), which is the result of adding to bombed out existing holdings and establishing some new ones, while existing holdings obviously shrunk in value. IASF's fixed income allocation (i.e. bonds with more than 1-year maturity) remains miniscule, yet high-yielding. Long option exposure was reduced amid a sale of a third of IASF's S&P 500 Dec 2020 Put options, while short option exposure is also reduced as current positions are not as deep in the money as last month. Cash and other liquid investments amount to 40.3%, which is virtually unchanged from last month.

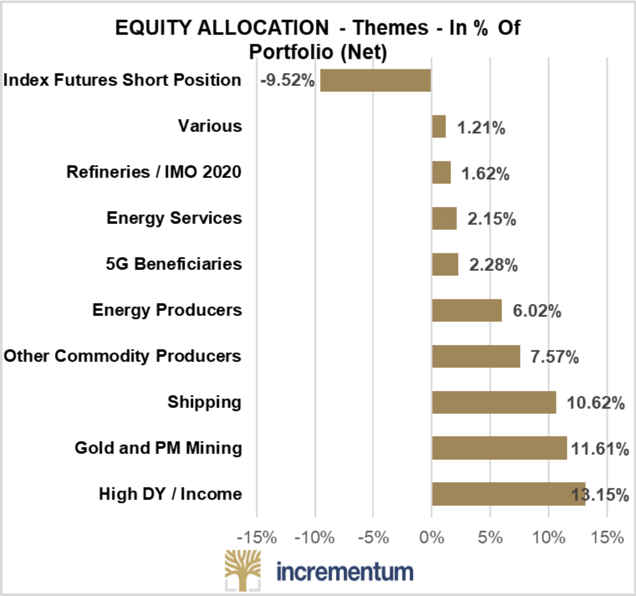
Asset Allocation



Currency Allocation

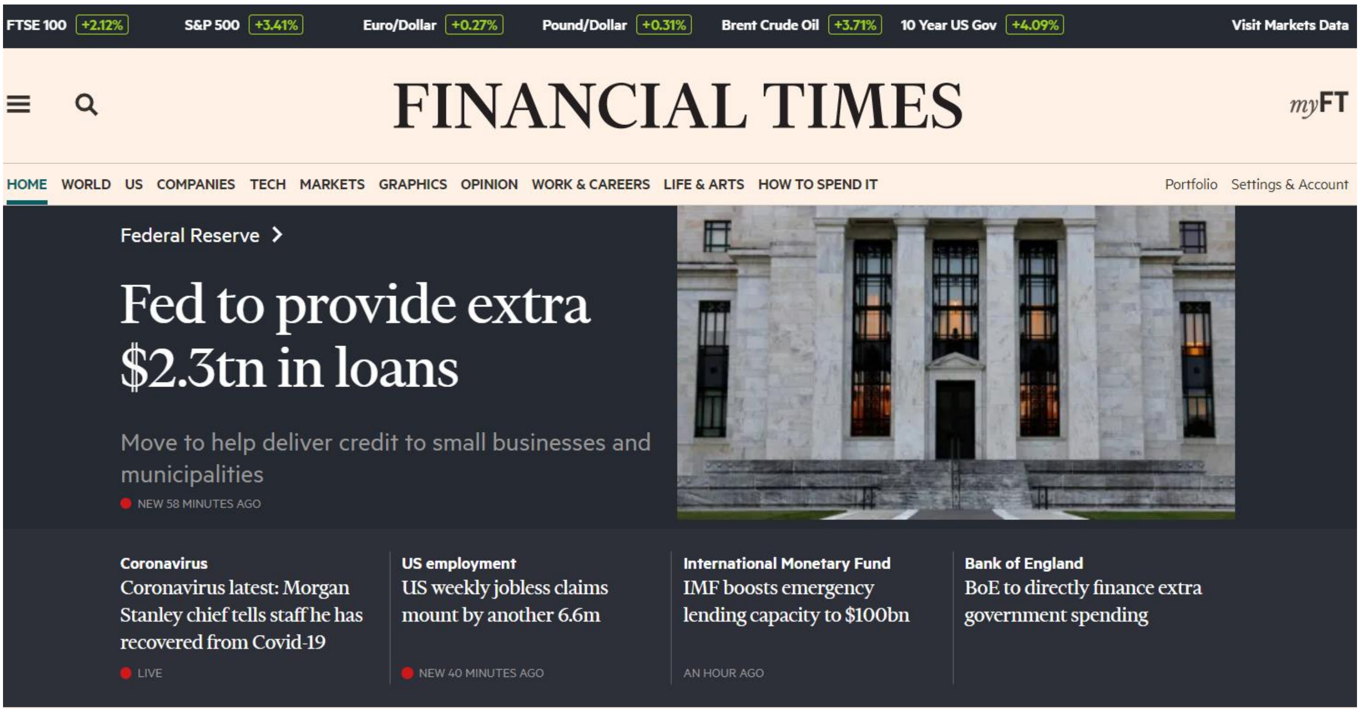


Currency allocation is still reasonably diversified, with the biggest changes in USD (+5%, amid a partial reduction in the existing hedge position), SEK (+3%, following exercise of a EUR/SEK Call option), GBP and Gold / XAU (+2%). As a result, the EUR allocation has fallen to 20% from 32% last month. Essentially, the portfolio has a third allocation to EUR and related currencies (NOK, SEK, DKK, CHF), a 28% allocation each to precious metals (via metals backed ETFs and miners) and the USD (mostly via USD/HKD based businesses / equities), and a 7% allocation to GBP, which seems rather undervalued, plus some further small exposures to CNY and SGD. I continue to regard this as appropriate given the uncertainty that the EUR as base currency of the portfolio is still facing concerning its longer-term future, which still hangs in the balance of so many divergent interests being tied together under one monetary roof.



In terms of IASF's equity allocation, the short S&P 500 futures position was closed during the March market decline, but is now being rebuilt amid the ongoing rebound. The biggest change among the equity themes is a 3% increase in the allocation to shipping stocks, where IASF has implemented an oil and product tanker allocation that is expected to benefit from the building oil oversupply. Meanwhile, the energy producer allocation has shrunk quite a bit amid the dramatic decline in share prices. Lastly, the gold and precious metals mining allocation has seen a small weight increase, mainly due to its outperformance.

In summary, March has been disappointing, as has been the 1Q 2020 performance. I now have 9 months to get the portfolio back into positive territory and so far, April looks promising in this regard, though this will be a major challenge. At the point of writing this in the afternoon of Thursday before Easter, the news is all about the authorities going all in to cushion the blow to the economy (see screenshot below from www.ft.com).



The question is: Will it be sufficient?

In Closing

This has been another long piece, which I hope readers have found worth their time spent on perusing. I know that at times this can have a tendency of sounding somewhat depressing, but I can assure you that I am quite optimistic that life will continue with and after CoV, and that markets will present us investors with some incredible opportunities down the road.

As far as a return to life after the CoV lock-down is concerned, I am convinced that people will be happy to go back to work, to see their friends and colleagues, and that they may get a changed perspective from all of this, perhaps finding more joy in the good things life has to offer and possibly even putting more value on their individual freedom as much as on solidarity with their fellow men.

But having entered the season of spring (at least in the Northern hemisphere) also should remind us that spring is a time of change. And I am greatly convinced that the world will have to change because as Albert Einstein is remembered to say: *"We cannot solve our problems with the same thinking that created them"*, which I believe is a quote that not only our political leaders and central bankers might want to reflect about.

I am certainly looking forward to what 2020 still has in store for all of us, and I look forward to hopefully meeting many of my investors and readers over the course of the year again. Until then I hope that you will all stay safe, healthy and in good spirits.

Wishing you all a Happy Easter!

Greetings from Schaan, Liechtenstein!

Best regards,

Hans

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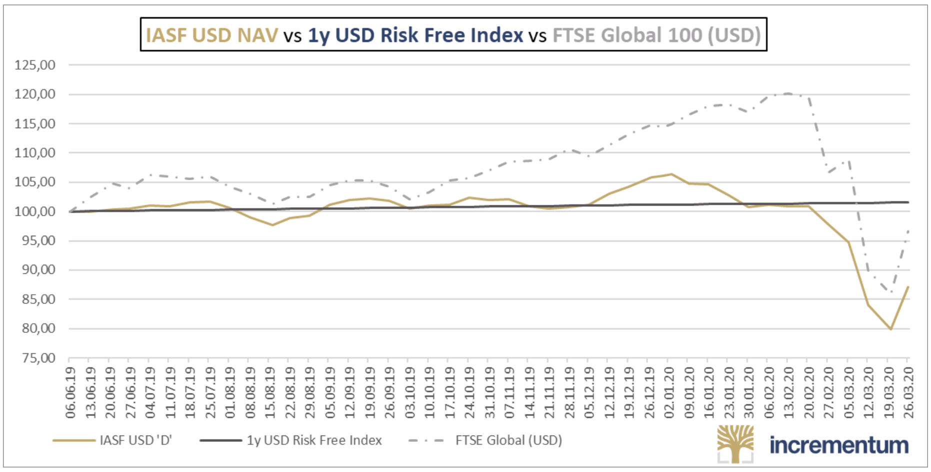
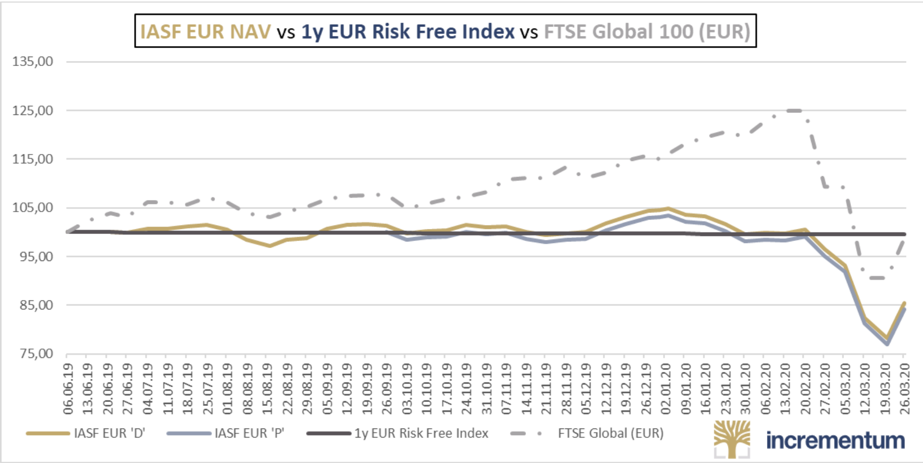
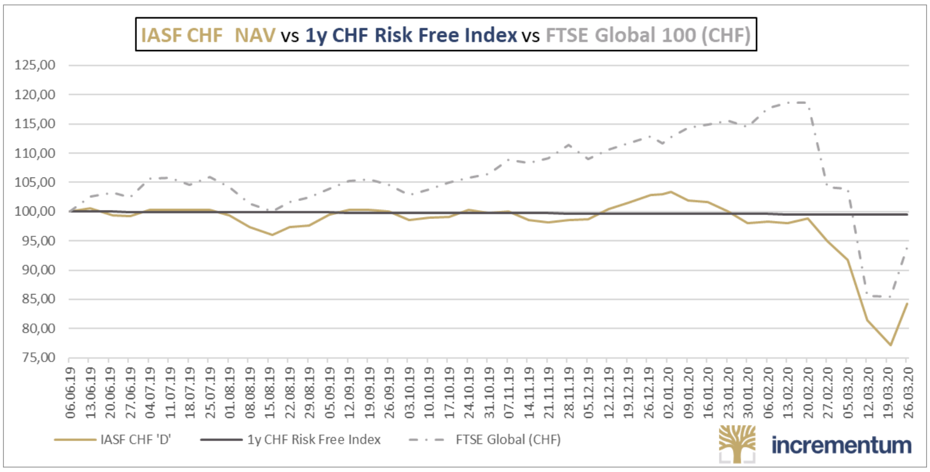
Appendix *







* Graphs display NAV of IASF 'D' shares as of last valuation date (**26Mar2020**), compared to the respective risk-free 1y-government yield as well as the FTSE Global 100 Index in respective currency as a proxy for overall equity market performance, from the start of the investment period (6Jun2019 for 'D' shares; 26Sep2019 for EUR-P shares) on an indexed basis.

IASF PM Shaped By 8 Investment Lessons

1. Capital markets, like the economy, are inherently cyclical in nature, and you must always know where you are in the cycle, while not hesitating to "Be fearful when others are greedy and greedy when others are fearful." (Quote: Warren Buffett)
2. Prices paid determine future returns, i.e. the higher valuations are, the lower future return expectations must be (and vice versa), which is the essence of value investing.
3. Capital preservation is the conditio sine qua non, and a consistent and long-term investment strategy is more important than short-term momentum chasing.
4. As a result you must always know when you trade, or when you invest.
5. The most basic and effective risk management tools are proper diversification and the ability to hold cash.
6. Hard assets are preferable to intangibles, distributions to accruals.
7. Look for the incentives: True alignment of interest works in investors' favor.
8. There is no magic formula for successful investing: Consider both macro- and micro-economic issues, be diligent, flexible, patient, keep an open mind, and realize that investing will always remain more of an art rather than a science.

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