


2020 / 05

May 2020

Seasonal Reflections

Investing in perilous times

quote(s) / chart(s), et al. of the month:

"What experience and history teach is this — that nations and governments have never learned anything from history, or acted upon any lessons they might have drawn from it." (Source: Georg Wilhelm Friedrich Hegel, from Lectures on the Philosophy of History (1832), Vol. 1, Wikiquote)

"The fall in oil is one of the markets' simplest, cleanest ways of saying that the global economy is in deep distress, and that manufacturers and airlines and households are not expecting to get back to business any time soon." (Source: The collapse in oil is a wake-up call for stock markets, FT, 21 APR 2020)

"With debt-to-GDP ratios expected to be significantly higher after the pandemic passes, monetary policy will likely have an important role to play in helping governments cope with the debt in ways other than outright default or recessionary austerity." (Source: Post-Pandemic Interest Rates, by Pimco's J. Fels, 13 APR 2020)

"Implicit in the world's Covid-19 policy response is that inflation (besides posing a less consequential risk than death by a novel virus) is not merely dormant but kaput. Count us in the dormant camp. The post-lockdown world — may it soon arrive! — will be one of reduced trade, stunted productivity growth and, if current trends hold, super-abundant monetary growth. And all of that in the context of the lowest interest rates in 4,000 years." (Source: A short history of making things worse, Grant's Interest Rate Observer, 1 MAY 2020)

"Time and time again, investors have demonstrated their willingness to buy equities in the knowledge/hope that central banks, and the Fed specifically, had their back. Yet there is zero evidence historically that markets can go up on a sustained basis whilst profits continue to slump. Equity markets may have bounced but investors still seem to be positioning themselves for a drop." (Source: Andrew Lapthorne at SocGen, FT Market Forces, Waiting for the lights to change, 20APR2020)

Headline of the Month: **Stimulus Oversight Panel Has One Person Trying to Watch $2.2 Trillion Alone,** Bloomberg, 14 APR 2020

Interview of the Month (2:37): ***"Chamath Palihapitiya on the U.S. coronavirus response"***, 9 APR 2020

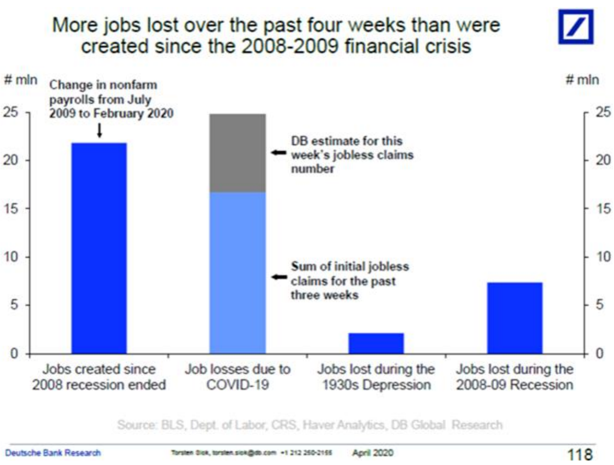
On the same subject (bailout culture): *"Rugged individualism and capitalism on the way up, privatizing the gains — and then socialism/cronyism on the way down as we socialize the losses with bailouts. … Since 2000, US airlines have declared bankruptcy 66 times. Despite the obvious vulnerability of the sector, boards/CEOs of the six largest airlines have spent 96% of their free cash flow on share buybacks, bolstering the share price and compensation of management … who now want a bailout. They should be allowed to fail."* (Capitalists or Cronyists?, by Scott Galloway, 10 APR 2020)

Worthwhile reads: The fear of coronavirus is changing our psychology (BBC Future, 2 APR 2020)

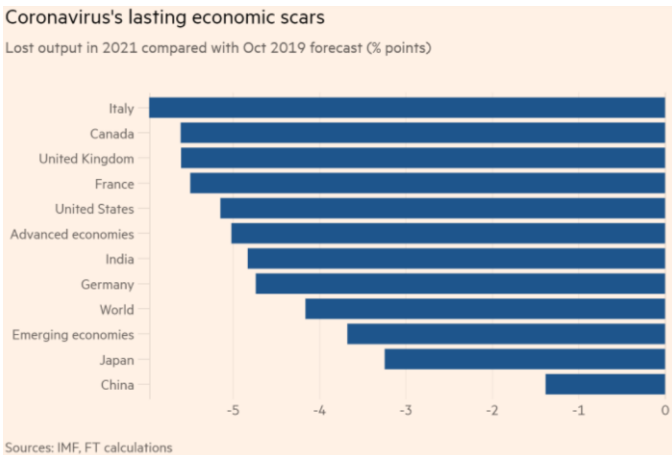
Must watch: About Black Swans, Gray Rhinos and Golden Bulls (World Gold Forum presentation by Incrementum Partner Ronni Stoeferle, 21 APR 2020)

Podcast of the month: Know Your Risk Radio – Zach Abraham interviews Grant Williams, 25 APR 2020

Charts of the Month:



Source: Torsten Sløk, DB, via The Big Picture, 14 Apr 2020



Source: Global economy to suffer worst blow since the 1930s, FT, 14 APR 2020

And as a reminder that there are other scourges than Covid-19, and for a little perspective: What the massive locust swarm in Africa and the Middle East means to the US, 21 MAR 2020

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Dear Reader,

I very much hope that my message finds you all in good health and spirit.

As you may recall I had planned to move towards a quarterly publishing schedule for my **Seasonal Reflections**, in light of their apparently unstoppable tendency to mushroom into almost book-sized form. But the past couple of months have once again served as a reminder that 95% of the time in the investment business are actually rather uneventful, while the remaining 5% is of the grey-hair-growth-inducing kind. At the start of this century's (roaring?) 20's, it seems we have entered the latter kind of period again, which tends to cause investors' sentiment to alternate between adrenalin rush and nervous breakdown. So, for now I am sticking to the monthly update schedule, while making another (with the knowledge of the final review, failed) attempt to keep this issue tight.

By early May the world is still struggling with the global Coronavirus (CoV) pandemic, and the threat it poses not only to our health but also - via the counter measures taken - to our material well-being and the stability of our societies.

I am sure most readers will have had their daily lives and routines quite severely disrupted in recent weeks, and apart from actual loss of job and income, angst levels concerning how the New (post COVID-19) Normal might look like seem rather elevated. Amidst all of this, however, it is easily forgotten though that eventually this shall also pass!

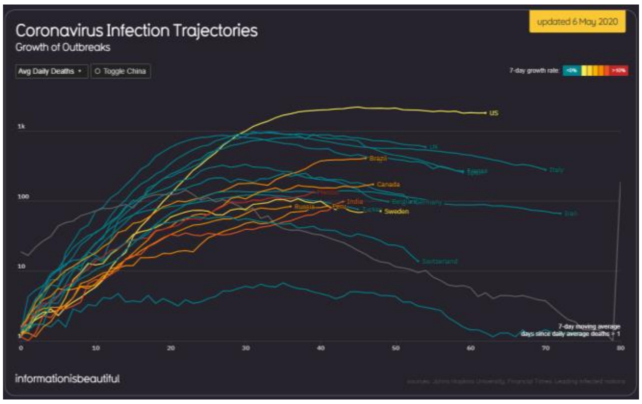
In fact, as is the mark of the season of spring, the world around us here in the Principality of Liechtenstein seems rather unimpressed by what is causing so much fear among us humans. Mother Nature has been showing itself from its most beautiful side in April, saturated with fresh colours and exploding with life, which personally always helps me adjusting my perspectives.

Source: HGS own pic, 18APR2020

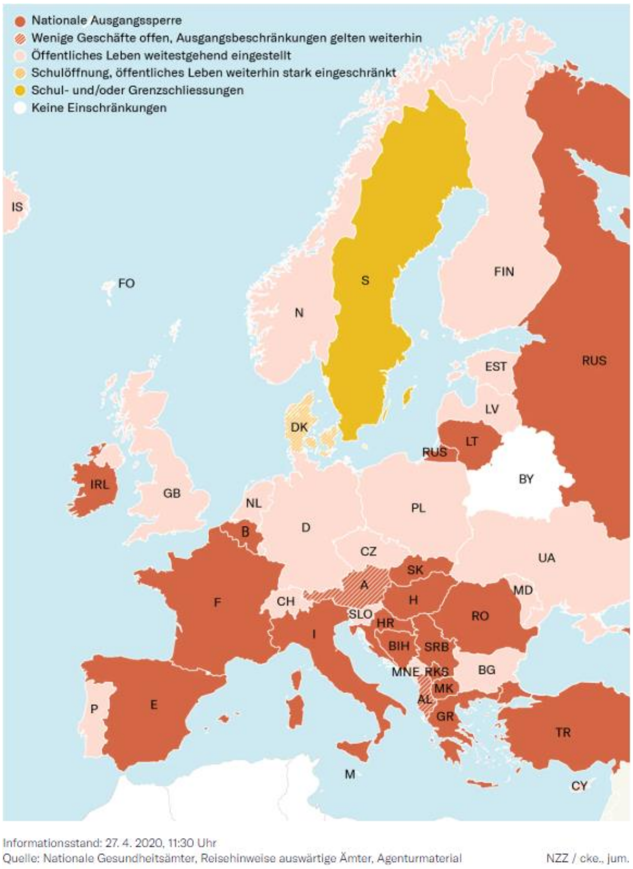
Like most of you, I have spent the past four weeks in mandated reclusion with my family, which meant I have been going to the office-office in the morning, while spending afternoons at my home-office. **Incrementum's** office here in Schaan is deserted as all partners work mostly from home, and the entire floor of our building has been mostly dark in April as other companies occupying it are doing the same. Traffic on the roads is greatly reduced, though as a first sign of a slow return to normality it has been picking up a bit during the first week of May. Fortunately, there has been no complete lock-down, which during an exceptionally dry and sunny month allowed us regular evening or weekend walks, one of which yielded the above photo. This greatly helped counter any acute development of claustrophobia.

That said, April was exceptionally reclusive. There were no visits from family and friends, no meals at local restaurants, no attendance of cinema or theatre performances, no going to the hairdresser - which despite of my wife's scissor'ed intervention has left me longer-haired (and bearded) - and no crossing the border to Austria, Germany or Italy. The emotional highlight of the week has become driving-lessons with my daughters on Saturdays on the deserted parking lot near Vaduz Stadium. In short, the world seems somewhat shrunk, a feeling many of you will certainly be able to relate to.

Overall, the CoV spread seems increasingly contained by now, as the slope of the average daily deaths' graphs in the log chart here suggests. According to Johns Hopkins University, total global confirmed CoV cases by May 6 came in at 3.666m, and that growth rate is clearly also slowing. This, however, was achieved at an increasingly evident cost. (By the way, informationisbeautiful.net provides a lot more interesting input on the CoV subject.)



Source: information is beautiful, 6MAY20



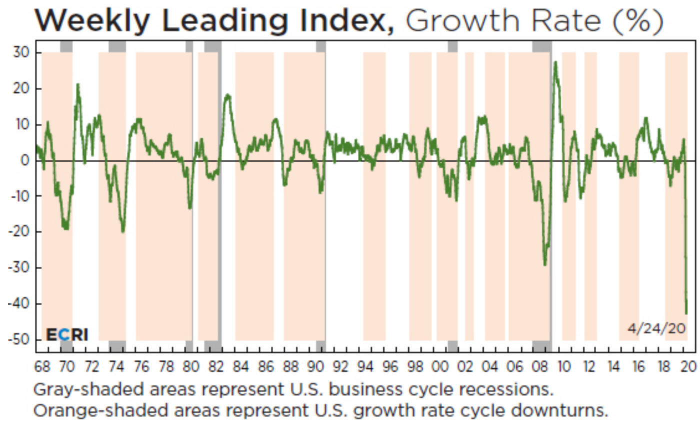
Source: NZZ, 3MAY20

Take Europe as an example. The map on the left, courtesy of Neue Zürcher Zeitung (NZZ), shows the various degrees of countermeasures implemented across Europe. Countries marked blood-red are in complete lock-down, whereas the more pinkish coloured countries have been less strict, though public life there is also mostly restricted. Belarus is the only country on this map, which had not introduced any restrictions, and according to the media with 17,500 confirmed cases has one of Europe's highest per-capita infection rates, though according to JHU the number of deaths so far (May 6) is "only" 107. Among Western European countries yellow-coloured Sweden has been the one with the most relaxed rules, and compared to its neighbours has seen a faster spread and somewhat higher death count, but also avoided the worst of the economic damage the lock-down measures have caused elsewhere.

So, let's look at some of the consequences of these containment measures? – In early April the International Labour Organization estimated that the CoV crisis will cut worldwide working hours by 7% in 2Q2020, *"a "catastrophic" effect that is equivalent to the loss of 195m full-time workers. The UN agency warned that 1.25bn workers — almost two-fifths of the 3.3 billion-strong global workforce — are employed in sectors suffering drastic falls in output, from retail and real estate to manufacturing, accommodation and food services. More than four-fifths of the global workforce live in countries where full or partial lockdown measures are in place."* (Source: Financial Times, 7APR2020) – These are staggering numbers, indeed…

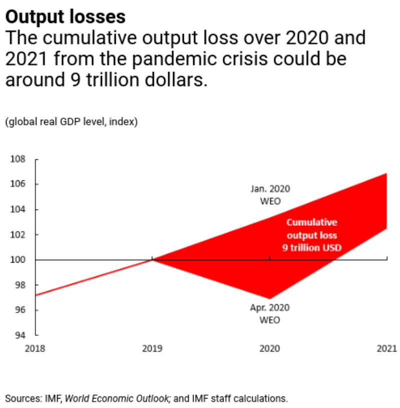
Eurozone business activity has been in free-fall across the board last month, and the same can be said for the ECRI US Leading Index, which has plummeted to lows not seen in half a century.

Source: Financial Times, 23APR2020



Source: Lakshman Achuthan, @businesscycle, Twitter, 1MAY20

Putting entire economies into mandated hibernation has caused an unprecedented demand shock. The EU Commission on May 6 published new GDP estimates which at -7.75% for 2020 came in far worse than the 4.5% contraction during the Great Financial Crisis (GFC). This compared to estimates from February which were still forecasting 1.2% GDP growth. Who under these circumstances does not recall the quip that it's tough to make predictions, especially about the future…

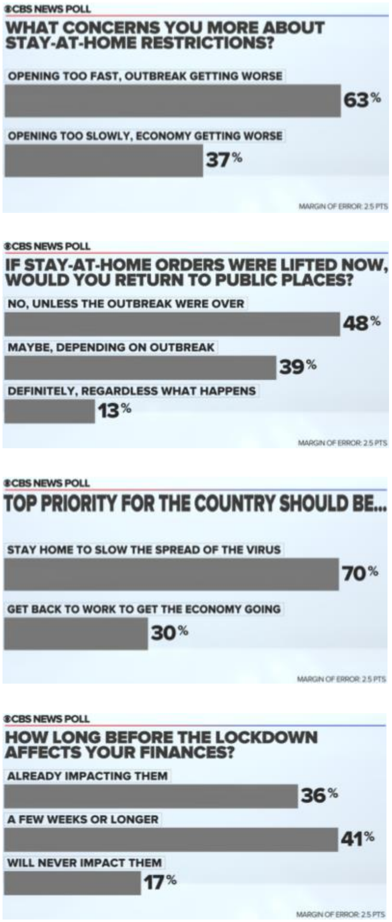


Source: FT Market Forces, 14Apr2020

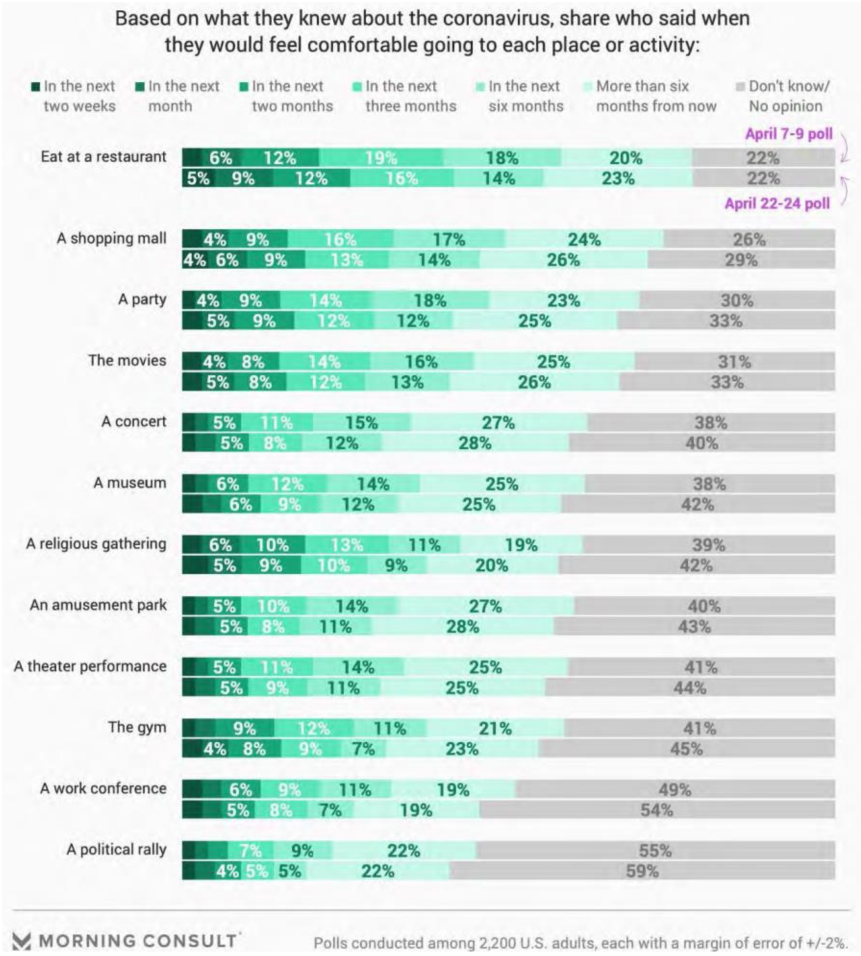
If people stay at home, they don't spend, and one person's spending is another one's income. As a result, job markets have been hit particularly hard, with many Europeans working reduced hours (e.g. 37% of Swiss employed (NZZ, 7MAY20)), while weekly jobless claims in the hire-and-fire US economy have accumulated to more than 33m people, which has destroyed 50% more jobs than were created over the past decade. And as employment creates confidence, creating consumer spending, creating growth, it does unfortunately also work in reverse. That is why in mid-April the IMF estimated a USD 9tr cumulative global output loss for 2020, a number greater than the combined output of Japan and Germany.

There should be no doubt that it is extremely difficult to come up with reliable numbers, mainly because this is such a unique slowdown. It is a bit like the global economy had been driving too fast and was suddenly forced to break hard to avoid hitting a roadblock. Such incidents cause an emotional shock that has one drive rather more carefully in the immediate aftermath. And so, I wonder whether wide-spread expectations of a quick rebound of economic growth are realistic.

In this context it is also important to recall that the slowdown was caused by a major public health crisis. I suppose everyone affected by the virus directly or indirectly via the containment measures will agree that human behaviour is probably going to change. Below are some recent polling results from the US which highlight at least the short-term sentiment. Does this suggest a V-shaped rebound in consumption to be even a remote possibility?



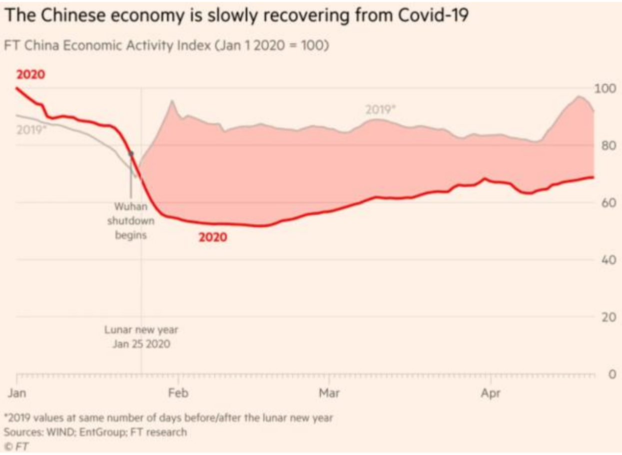
Source: Americans prioritize staying home, via [CBS](), 23APR2020

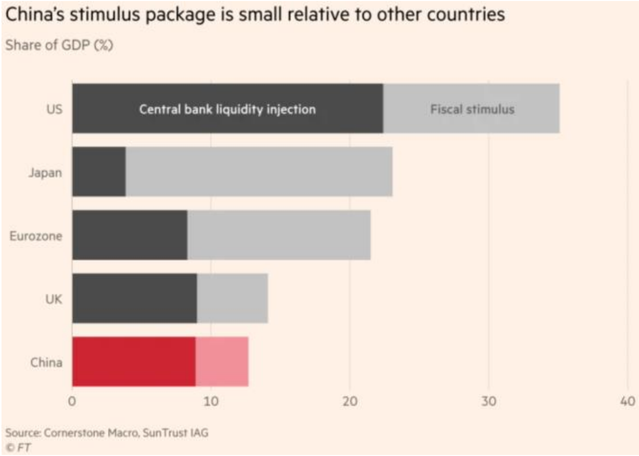


Source: Business As Usual by TIS Group, 30APR2020

So, we have seen an unprecedented collapse in demand, leading to expectations of the deepest recession since the Great Depression. Clearly, time to dust off those monetary and fiscal bazookas or better yet the entire artillery…

China was obviously first in and out of the crisis, though the getting "out" process seems a little bit slower than the going "in", which again might provide us with more than a hint about the shape and speed of the recovery.





Source (for both): Financial Times, 22APR20

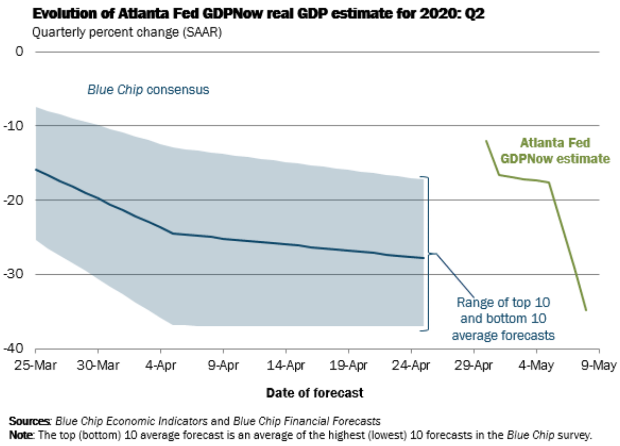
Of course, contrary to 2008/09 China has actually been the most cautious in its response to the crisis, with the combined "stimulus" at about 12% of GDP. This is dwarfed by combined stimulus exceeding 20% for the Eurozone and Japan, and well over 30% in the US, where however the Fed has to do most of the heavy lifting, while Europe and Japan have overweighed fiscal stimulus.

Source: investing.com, 18MAR2020

Though the numbers on first glance would suggest a massive boost to GDP, this is not really stimulus. In fact, there is not much to stimulate given that the economy is shuttered. Instead, a major part of the government intervention is directed at staving off the day when a liquidity pinch for companies becomes a solvency crisis, while trying to compensate households for a sudden loss of employment income, all funded by newly minted dollars.

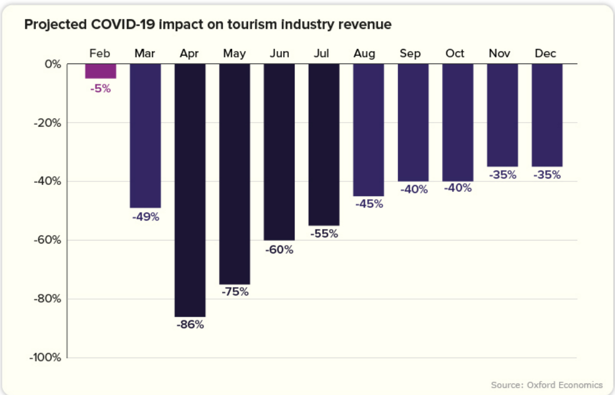
Take the US CARES act as an example: It pays out an additional USD 600 per week to top up average weekly unemployment benefits (about USD 300 p.w.), which according to CNBC seems to have led many low-income earners to prefer being on the dole rather than labouring for a lower income. Though it has helped support household demand short-term, it is another step towards a socialist type of redistribution, where the masses increasingly rely on government handouts funded by monetary inflation. The CARES act expires July 31 but may prove a precedent for moves towards UBI (Universal Basic Income) or other so-called MMT (Modern Monetary Theory) measures.

Meanwhile, economic activity is still contracting seriously, with the Atlanta Fed's GDPNow tracker on May 8 estimating an annualized **35% (!!!)** GDP contraction for 2Q 2020, which is basically double the shrinkage that was expected a week earlier. No doubt, these numbers tend to be extremely volatile, and are likely to bounce back in the weeks to come, but we are clearly in unchartered territory. I am quite convinced that the real economic damage will only slowly become evident.



Source: https://www.frbatlanta.org/cqer/research/gdpnow

The trouble is that politicians have decided to centrally plan the economy and life of their citizens, and this type of micro-management is bound to be inefficient, as every additional rule and regulation comes with its own set of unintended and likely unforeseen side-effects.



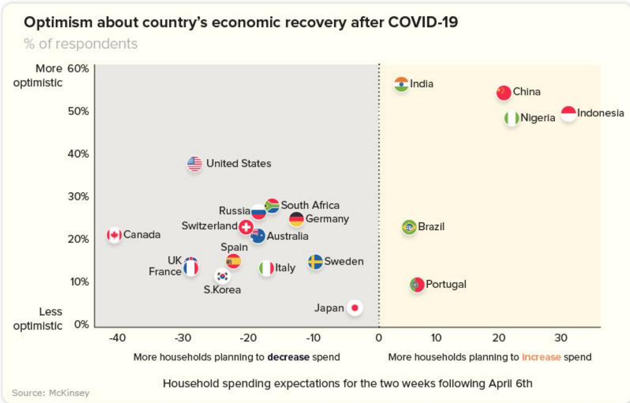
Source: Visual Capitalist, 22APR2020

Take the tourism industry as an example. According to the World Travel and Tourism Council, a staggering 50 million jobs are at risk in the industry, with two-thirds of those belonging to employees in Asia. Considering the travel and tourism industry accounts for 10.4% of global GDP, a slow recovery as forecasted by Oxford Economics in the accompanying graph will have serious ramifications for overall GDP growth.

And yet EU Commission president Ursula von der Leyen suggested last month that no one should be planning a summer break. Given that tourism also counts for an estimated 10% of EU GDP, the political backlash was fierce, and now the administrators of our self-inflicted economic depression are struggling to come up with suitable adjustments and are increasingly overwhelmed by the task of finding a compromise between the varying interests. And the same struggle is taking place across many other sectors of the economy and in most parts of the world.

Similar to tourism (and travel) the measures to contain the virus have led to big job losses to be registered in leisure, hospitality and personal services, but also across sectors as diverse as professional services, manufacturing, construction, media, etc. Based on past experiences, the assumption is that the resulting job losses will prove temporary. But an ongoing public health scare, coupled with the demand-driven nature of this recession may make past experiences an unsuitable blueprint this time around.

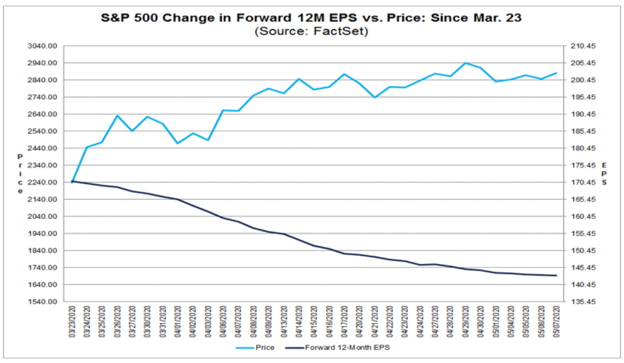
Personally, I believe it is inevitable that all of this will have a dramatically negative impact on consumer spending. I invite readers to provide me (email: hgs) with a feedback on their own personal spending patterns over the past few months, and their expectations for the same going forward. First polls concerning the subject are hardly encouraging, and thus one can only conclude that consumer spending will take time to recover to pre-CoV levels.



Source: Visual Capitalist, 22APR2020

This also because economic crises like the one we experience right now tend to lead to a rise in household savings ratios. An Allianz economist recently predicted that consumers are expected to increase their savings, even after the lockdowns are lifted: *"We think we will see €1.3tn of additional saving in the EU — a 20 percentage point increase in the household savings rate in the second quarter alone — which is the effect of people not being able to spend and also being more cautious when the lockdown is lifted,"* she said." (Source: Katharina Utermöhl, economist at Allianz, Financial Times, 23APR2020)

Meanwhile, for the corporate sector 1Q earnings season was nothing to cheer about, and even less so if one focused on the outlook section. According to an IFO survey in April about 84% of companies in Europe reported a decline in **sales** due to CoV, and less than half reckon they can make up for this in the future. It is worth to recall here that a shrinking top-line typically results in an even faster shrinkage of the bottom-line… - In addition, there is plenty of evidence of supply chain problems, as global manufacturing had already been upset by the trade war and received an even worse blow from CoV.



Source: Sven Henrich, @NorthmanTrader, Twitter, 12May2020

Consequently, the trend for 12-months forward earnings has been coming down lately, an usually optimistic analyst community notwithstanding. However, as the graph on the left also shows that has not stopped equity prices to go up, a phenomenon the author of this tweet describes as "*Multiple expansion in print*". And this brings me to my core dilemma as investment manager.

Although the investing environment over the past four weeks offered more than enough variety (aka volatility) and stimulus to make up for the quiet life experienced under social distancing and officially mandated isolation, the disconnect between real world news and developments from what financial markets are apparently pricing in is hard to fathom, and has proven exceedingly challenging.

To us as professional investors, April has put into stark relief the world we live in. What do they say? – I guess, a picture says more than a thousand words….

I know equity markets are discounting mechanisms, and powerful counter-trend rallies can often occur while economic news is still deteriorating. But witnessing the first hints about the damage the fight against CoV is causing to our economies, with no certainty how bad things are going to get in the coming months, and watching the buy-the-dip reflex springing into action again, has been truly disconcerting. It makes me wonder what the process we call "investing" has become?

Source: Desk_Jockey, @jockey_desk, Twitter, 10APR2020

We used to have true markets, where mostly private, but always profit- / return-driven investors were trying to decide where best to put their scarce capital to work, i.e. where they were likely to achieve decent risk-adjusted returns. That meant analysing individual investments concerning their credit quality / balance-sheet strength, intrinsic value and dividend / coupon distributions, and only then concerning their growth expectations. The worse the outcome of such an analysis and the grater the uncertainty, the lower the price an investor was prepared to pay for such an investment, because it was understood that ones' capital was at risk of being lost.

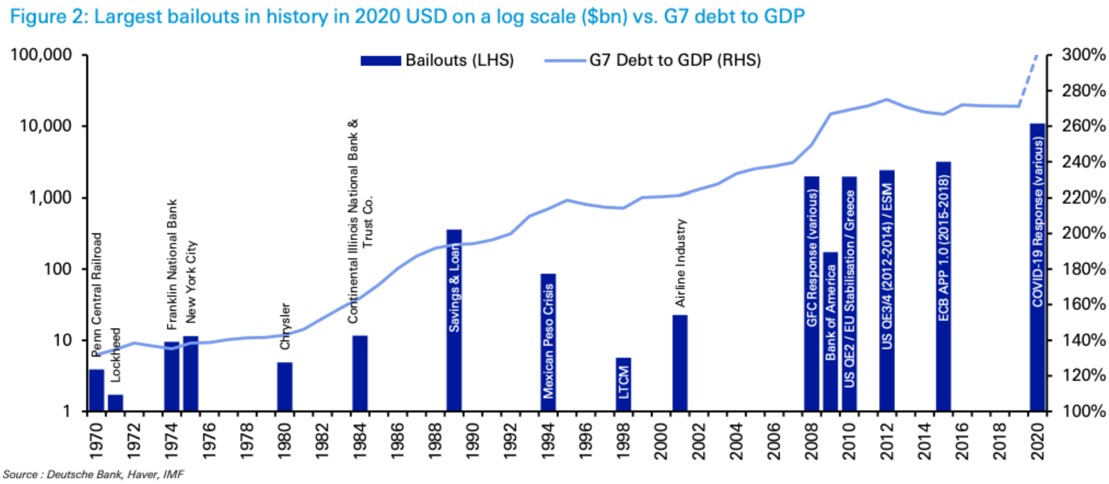
In addition, there was also always a positive risk-free return on offer, which presented the opportunity cost / benchmark against which any investment opportunity was compared. And if investors felt uncomfortable with the risk-/return sets offered, they could just keep their powder dry and wait for better opportunities to come along WITHOUT risking ongoing and systematic real (inflation-adjusted) destruction of their capital.

I know these days this sounds almost like a fairy-tale, but overall this was how investing used to work, and it was a much fairer system than today's so-called financial "markets", which have essentially morphed into political utilities. These utilities are increasingly and openly manipulated by central bank interventions, ultimately serving both as measure of success for a sitting US president, as well as in order to avoid exposure of the rotten state advanced economies retirement systems are in, and of course most of all to prevent the implosion of the biggest debt bubble the world has ever seen. Today, everything is done with the ultimate goal of kicking the can a little further down the road, and to prop up an increasingly fragile economic, financial and monetary system, and we have long ago stopped counting the cost.

Source: [Hedgeye](), 27APR2020

The above described changes have been the result of countless political decisions made over the past decades, and have turned financial markets, which were once the bastion of capitalism, into a socialist planning system that is increasingly distanced from reality. And as price insensitive central banks have become the largest buyer in financial markets, most investors have obviously followed their lead.

"In a matter of weeks, policymakers have become a backstop for private-sector credit markets. At the extreme, central banks could become permanent command economy agents administering equity and credit prices, aggressively subduing financial shocks. With unlimited capacity to print money, central banks have unlimited capacity to intervene in asset markets too. Put simply, a central bank that pegs bond, credit and equity markets is highly likely to stabilize portfolio flows as well." (Source: Deutsche Bank's George Saravelos in an FX Strategy piece, quoted in [Seeking Alpha](), 26APR20209



Source: [Dystopia Now](), Seeking Alpha, 26APR2020

"Economic data and asset prices ostensibly reflect something real, whether that means the production of goods, the provision of services, cash flows, operating income or even sentiment, which, while hard to measure, is real too.

Although monetary accommodation in the post-GFC world impaired price discovery, we mostly spoke in terms of engineered disconnects between prices and fundamentals. In some cases, those disconnects became patently absurd. For example, some European corporates saw their entire (yield) curves go negative last summer, which effectively meant that for those companies, debt had become an asset. Sovereigns which had no business tapping the market at all based on fundamentals were able to borrow at what, just a decade ago, would have been low rates even for a developed economy. And on, and on.

But, in all cases, there was still something there. The prices for fixed income may not have represented the risk associated with a given borrower, and equities were of course distorted by the very same dynamics (as the voracious appetite for corporate issuance allowed management teams to plow the proceeds from record bond sales into EPS-inflating buybacks), yet through it all, sovereign borrowers still had tax bases. There was still an economy to reference. Corporations, even unprofitable ones, still had operations.

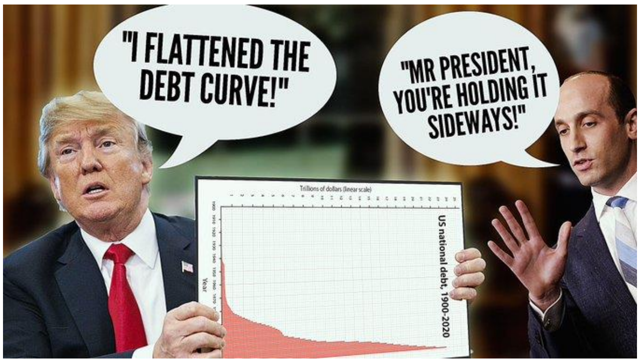
Now, there's a very real sense in which the underlying "stuff" (so to speak) does not exist. Economies are shuttered. Tax payments have been delayed. Rather than take in revenue, governments are handing out cash. Businesses are idled. Corporate titan after corporate titan is withdrawing guidance.

This is a temporary state of affairs, but the point is simply that some of the assets you own are, for the time being anyway, claims on things that don't exist." (Source: Dystopia Now, Seeking Alpha, 26APR2020)

The point I am trying to make is that we are in truly unchartered territory. Admittedly, I felt the same in 08/09, when the house of cards was stabilized by what was then considered truly unprecedented bailout measures. This time around, the committee to save the world has reacted fast, indeed. But last time they merely had to bail-out the financial system, while this time they got to substitute a demand shock of epic proportion. That cannot be done by Quantitative Easing, i.e. the accumulation of financial ~~assets~~ claims alone.

Source: Investing.com, 30APR2020

Consumers were forced to stop spending and have hunkered down at home. This has had the business sector collapse into the worst recession in a century, which resulted in gargantuan bailout programs. Centrally planned these typically come with plenty of moral hazard in tow, as the 2008/09 bailout already amply demonstrated. Last month for example, the Financial Times reported that Delta Air Lines received a total aid package worth USD 5.4bn, consisting of a USD 3.8bn grant (i.e. taxpayer funded subsidy), a USD 1.6bn unsecured loan carrying a modest 2% interest, plus warrants which represent a grand 1% of the company's equity at a strike price reflecting Delta's April 14 closing price of USD 24.39. The FT's *"Sujeet Indap did some illustrative maths to show that given the modest equity sweetener and a mostly free subsidy to Delta, the US taxpayer would almost certainly be earning a negative rate of return. The break-even point occurs if, after 10 years, Delta shares rocket from $24 today to $560."* (Source: Financial Times, 16APR2020) – In my humble opinion, this is simply scandalous, considering we are talking about a company that in the last six years has returned $60bn in stock buybacks and dividends, thus depleting any reserves that could have helped it weather the storm this time.

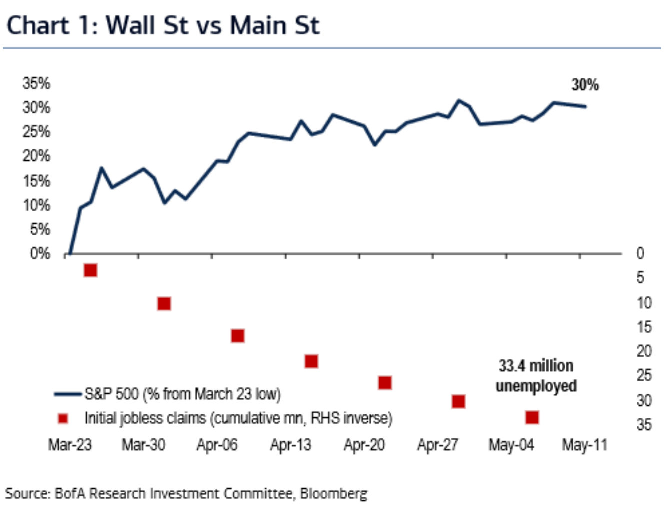


Source: Mark J. Valek, @MarkValek, Twitter, 22APR2020

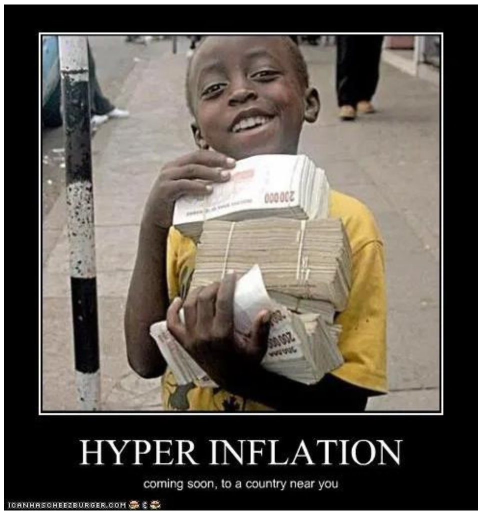
I doubt the current economic malaise can be fixed by buying bonds or even equities, and I am not sure it can be compensated for by QE for the people, i.e. transfers to households, even if it is coupled with government spending, although it seems that especially the USA under their fearless leader are making every effort to prove me wrong – any long-term consequences for the nation's solvency be damned…

But this is the treacherous terrain investors need to navigate these days. Market valuations have completely decoupled from underlying business fundamentals, as corporate profits are privatized (though disproportionately to corporate managements) and business risks and losses are born by taxpayers. (The 2 opening pages contain plenty of additional evidence on the subject.)

Financial markets do not share my worries yet, as the chart on the left below suggests. They are obviously convinced that the central banks and governments in their perceived omnipotence can bail the system out once more. – The question is at what price?



Source: Jeroen Blokland, @jsblokland, Twitter, 12MAY2020



Source: Adventures in Capitalism, 5APR2020

I know it has become rather old-fashioned to worry about inflation. For now, and recalling my opening thoughts on the ever expanding content of these **"Reflections"**, I will leave the subject to Incrementum partners Ronni Stöferle and Mark Valek, who in their upcoming In Gold We Trust report **"The Golden Decade is Dawning"** to be published on May 27, will as usual report extensively on the ongoing monetary debasement. But I want to leave you all with a simple thought: If money printing can create economic wealth and prosperity, why is Zimbabwe not the most prosperous nation on earth?

Before I continue with more observations related to the **Incrementum All Seasons Fund**, please do take note of the following:

Any investment analysis, views, 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 an 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.

Ok, with this out of the way…

What do we do as fund managers, whose aim is to prudently invest the money entrusted to us?

With central banks buying up all the (public and increasingly private) debt, and governments throwing out any residual constraint on more debt funded spending (now of course all in the name of fighting the virus), investors are once again under the spell of TINA (**T**here **I**s **N**o **Al**ternative (to equities, that is)). This at least partly explains the significant rebound we have witnessed in equity markets last month.

Source: [Grants Interest Rate Observer](), Vol. 38, No. 10, May 15, 2020

Do we follow the crowd and hope that the mirage of unending wealth can be extended ad infinitum? – Isn't this the ultimate hyper-inflation, where increasing amounts of money are bidding up an existing stock of financial claims (I think the expression asset purchase (programs), which our monetary mandarin's prefer to use, is a gross misdirection) and equity shares in businesses, as well as real estate, art, etc.?

Source: [www.investing.com]()

Sure, those who participated in just putting their money into the fabulous FAAAM (**F**acebook, **A**pple, **A**lphabet, **A**mazon and **M**icrosoft now account for about 21% resp. 45% of the S&P500 resp. Nasdaq 100) have enjoyed ever-increasing paper profits. But should we as your fiduciary manager jump on that train now, hoping that these mega-companies will ever see their revenue growth and profitability catch up with the prices paid today?

To be frank, any active fund manager, and especially if he has pursued a value approach to investing, will have asked himself that question many times in recent years. And so have I! – But to me personally, bearing responsibility for money invested in the **Incrementum All Seasons Fund**, this was never an option. – Why? – Because deep down I remain convinced that "investing" as I have described it on page 10 above is not dead. Investing needs a story, embedded in a future scenario, but most importantly a valuation assessment, which tells me that what I am buying is cheap compared to what my analysis finds it is worth. Sometimes, that future scenario does not come to pass, as happened during 1Q 2020 with my expectations concerning the development of energy demand and thus prices. These severely undershot even my worst nightmare expectations, and thus caused a dramatic fall in related share prices. But equity shares in businesses are always long-term in nature, and I have no doubt that given sufficient time I will still extract value for the fund's investors from my selections. And if I find my assessment faulty, which of course also happens, I will not hesitate to liquidate related positions.

There is another important aspect to highlight here. On the fund's homepage the first sentence is: The **Incementum All Seasons Fund** is a strategy fund, which aims for real (i.e. inflation-adjusted) NAV growth over the duration of a market cycle. A market cycle typically lasts about 5 years, though arguably the current one (the bull started in March 2009 and ended February 2020, while the bear phase is still ongoing) has achieved an unusually long and record duration.

At the time of writing, **IASF** is not even 1 year old, but we managed to achieve an inflation-adjusted positive return for the calendar year 2019, despite of the fact that the fund had little more than 6 months in 2019 to get seeded and invested, i.e. to build the portfolio into the desired allocation, which as any active investment manager will know does tend to take a bit of time.

IASF 2019 NAV Change

6.6.(D)/26.9.(EUR-P)-31.12.2019

EUR-D	104.49	4.49%
USD-D	106.08	6.08%
CHF-D	102.96	2.96%
EUR-P	103.02	3.02%

For Charts, See Appendix

IASF Year-To-Date NAV Change

31.12.2019 - 30.04.2020

EUR-D	93.81	-10.22%
USD-D	95.30	-10.16%
CHF-D	92.23	-10.42%
EUR-P	92.35	-10.36%

For Charts, See Appendix

2020 so far has been a disappointment, especially after I had raised expectations with my confidence that the fund's NAV would prove resilient in an equity market correction. This – at least in the short-term – was a promise the fund has not been able to keep. But it is still early in the year, and of course we are still a long way from concluding a whole market and investment cycle.

However, it is clearly inappropriate to compare **IASF** with a simple long-only equity portfolio or index. Even if the fund's main risk asset exposure currently is to equities, it might own 100% bonds in a different investment environment. After all, the fund aims to achieve real (i.e. inflation-adjusted) NAV growth over the duration of a market cycle, not to beat an equity market benchmark. Given the diversified nature of the fund's assets and the tendency to maintain cash over the cycle this will generally make the fund more defensive in risk asset downturns, even if I failed to deliver on that in 1Q 2020.

Some investors may argue that they do not care about the investment approach, because all that matters is investment results, and I would obviously agree with that. But any comparison should be apples to apples, while the establishment of a reliable track record requires both time and consistency. I hope to be granted the first in order to deliver on the second.

Now, let's look at how **IASF** has fared in April. As indicated earlier already, **IASF's** NAV rose almost 10% last month, thus recovering almost the entire loss we had seen in March. The slight performance differences between the various share classes shown in the accompanying table are due to the fact that USD and CHF share classes are not always entirely hedged back into EUR.

IASF Month-Over-Month NAV Change

April 2020 (26.3.-30.4.)

EUR-D	93.81	9.72%
USD-D	95.30	9.38%
CHF-D	92.23	9.41%
EUR-P	92.35	9.67%

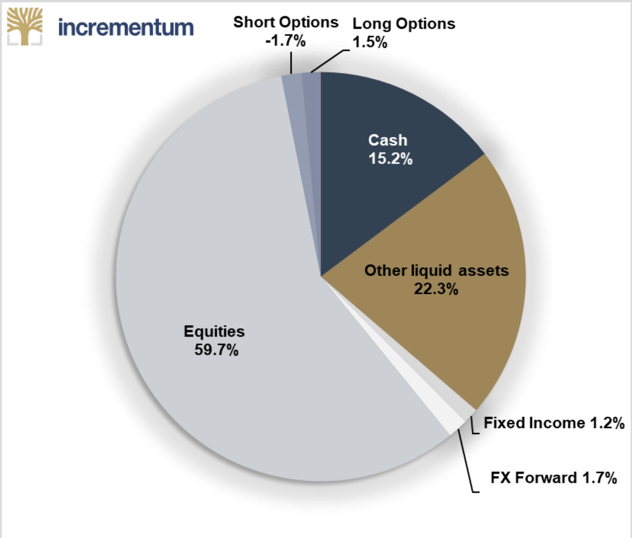
For Charts, See Appendix

Given the substantial swings witnessed in the fund's asset base over the past few months, we aim to keep hedges within a 5% range. In April, the USD rallied versus the EUR base currency of the fund's portfolio, and the shortfall in the underlying hedge position thus caused the USD tranche to underperform. However, such deviations should even out over time.

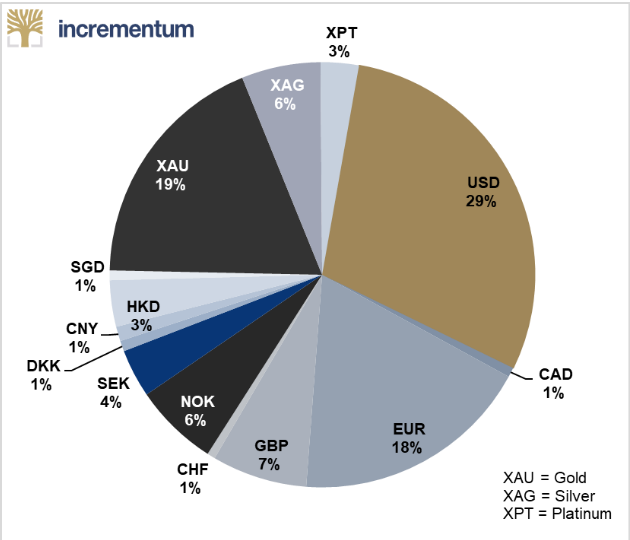
So, with this out of the way, let's look at **IASF's** portfolio positioning at the end of the month. The fund's net assets stood at EUR 41.8m (USD 45.3 / CHF 44.1m), and there was only one small inflow of EUR 25k in April.

End of April allocations are as usual displayed in the accompanying graphs. They show a slight increase in equity allocation to 59.7% (+3.5%), which was mainly performance driven. **IASF's** fixed income allocation (i.e. bonds with more than 1-year maturity) remains miniscule, yet high-yielding and volatile. Long option exposure shrunk as the remaining S&P 500 Dec 2020 Put options declined significantly in value, while short option exposure was more or less unchanged. Cash and other liquid investments came in at 37.5%, which amid the rally in risk asset prices and thus net assets caused the liquidity weight to drop by 2.8%.

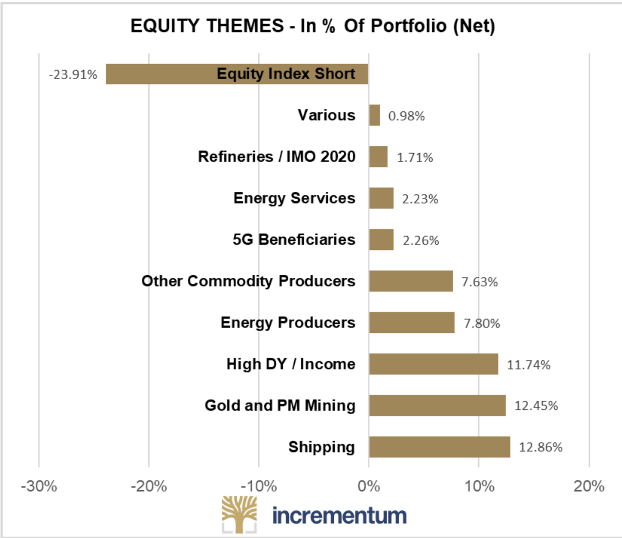
Asset Allocation



Currency Allocation



Currency allocation remains well diversified, with the biggest changes in USD (+4%), amid a rise in the value of USD assets and the purchase of USD based Frontline stock on the Norway Stock Exchange using NOK cash. At the same time, NOK and EUR allocations fell by 2%, the former due to the Frontline purchase, the latter performance driven. Precious metals allocation remained largely unchanged, as a third of the fund's Newmont Mining position was liquidated via execution of covered calls that expired in April. A similarly sized call was sold for May with a 20% higher strike (USD 60) which is likely to be called tomorrow as well.



In terms of the fund's equity theme allocation, the short S&P 500 futures position was increased to 23.9% (from 9.5%) at an average 2820 entry level. – On the long side, the biggest changes occurred in **Shipping** stocks (+2.2%), where the tanker exposure was built out, while **Energy Producers** (+1.6%) and **Gold and PM Mining** (+0.8%) enjoyed an uplift in prices (despite of profit-taking), while the **High DY / Income** allocation fell by 1.4% due to the sale of China Mobile via covered call exercise, and due to additional partial profit-taking.

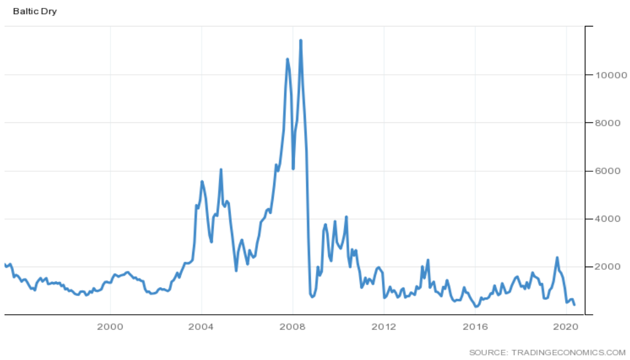
In summary, April portfolio action provided some relief following the serious correction suffered during 1Q 2020, and I am generally satisfied with how the portfolio has developed in April. Our overall management approach has adapted to the altered volatility environment. One notable change has been the uptick in the pace of selling equity options, which over the past four months has yielded approx. 1.5% in premium income based on the fund's net assets, even though on average less than 10% of portfolio assets were exposed to these options. Particularly attractive premiums were harvested in above mentioned tanker stocks (both puts and calls), by selling gold mining calls, and in the high octane energy space. Here, for example, call options sold on ¼ of the fund's position in Antero Resources already yielded 27% of the purchase cost for the underlying shares in one month, though half of the position may be exercised at USD 2.50 on May 15, more than double the "last-in" purchase made in the stock.

Given that **Shipping** has become the largest equity theme within the fund, let me quickly highlight what is driving this allocation. A recent headline in an Arctic Securities sector report was "*If it wasn't volatile, it wouldn't be shipping*", which I believe sums current conditions up perfectly!

Source: Hedgeye, 7JAN2020

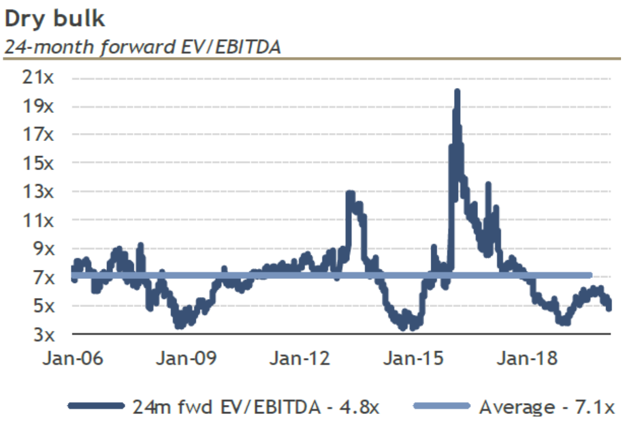
IASF has had exposure to the bombed out dry bulk shipping sector for a while, given stocks in this sector are trading at significant discounts (currently on average 70%) to book value and NAV. For investors concerned about currency debasement and a transition to a more stagflationary environment, buying long-lived assets at such steep discounts to (current) replacement cost should be tempting.

But the green shoots witnessed during 2H 2020, when the Baltic Dry Index reached 5-year highs, have been entirely crushed again amid the current global economic slowdown. At the time of writing, dry bulk shipping rates are probing their 5-year lows amid a reduced need for transportation and general logistic supply disruptions, though the graph on the right also highlights the extreme cyclicality of this sector.



Baltic Dry Index, Source: tradingeconomics.com

But with governments around the world throwing all hesitation concerning debt funded stimulus overboard, and increasingly resorting to actual demand boosting measures, we expect a significant recovery over 2H 2020. For now, however, it is extremely challenging to be a bulker owner, as current rates do not even cover OPEX. As a result, an already thin new order book is slimming down further.

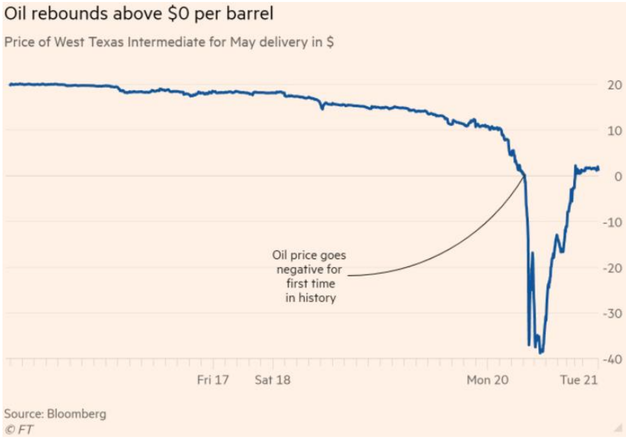


Source: Arctic Securities, Shipping Sector Report, 24APR20

Having said that, we have so far left our exposure largely unchanged this year, making only small add-ons to Pacific Basin and Eagle Bulk, which leaves overall exposure to the dry bulk sub-sector at 4.4% (not counting Nippon Yusen, which is a diversified shipping co.). Given cyclically depressed valuations, we might consider further additions once the cycle is decisively turning, though this is usually also accompanied by rapidly rising share prices.

A quick word on **IASF's** tanker basket (6.3% of assets), which was accumulated over the past 3 months, and is comprised of market leading stocks like Euronav, DHT, Frontline or Scorpio Tankers.

Tanker rates have been soaring during 1Q 2020, as the CoV containment measures caused an extremely sharp drop in crude oil and refined product demand, while supply was initially boosted with the Saudi price war declaration, after OPEC+ could not agree on supply cuts. The result was the April drop for the history books, which saw WTI futures fall to as low as USD -40; in other words holders of long future positions were paying buyers to take oil off their hands given limited access to storage.

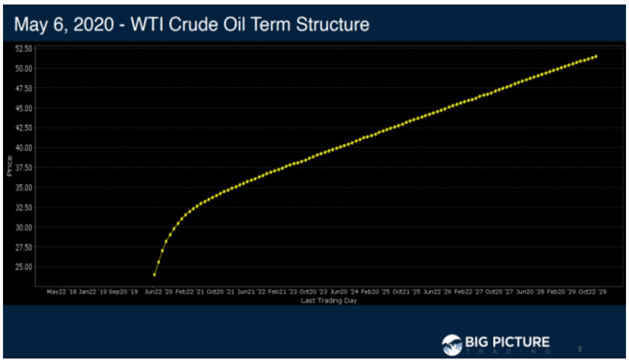


Source: Financial Times, 21APR2020

Source: Hedgeye, 20APR2020

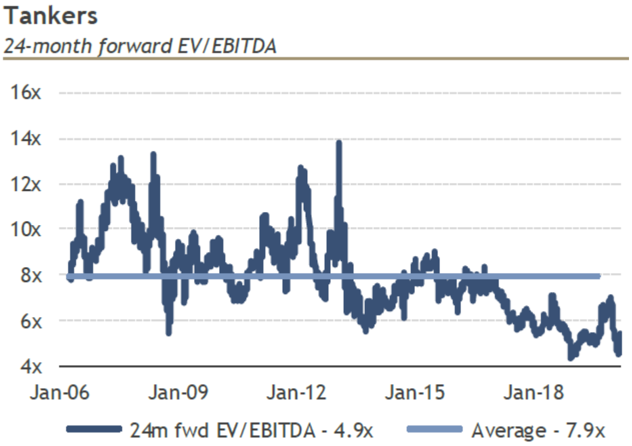
It is safe to assume that this was a shock to the entire industry which caused a fairly rapid reassessment, and under the cover of political pressure which helped hiding the plain truth that no oil producer can afford to stay in the business for long at prices below USD 30 – let alone at zero or below – sizeable production cuts have by now been implemented, both by OPEC+ and non-OPEC members, including the USA.

With global onshore storage facilities already filled up to the brim, the supply surplus caused growing demand for offshore / seaborn storage. And with oil futures in contango, i.e. prices at later delivery dates more expensive than the respective earlier delivery dates, the incentive to buy oil cheap and sell it forward at a more expensive price, while hiring tankers to store the oil in the meantime, led to record high charter rates.



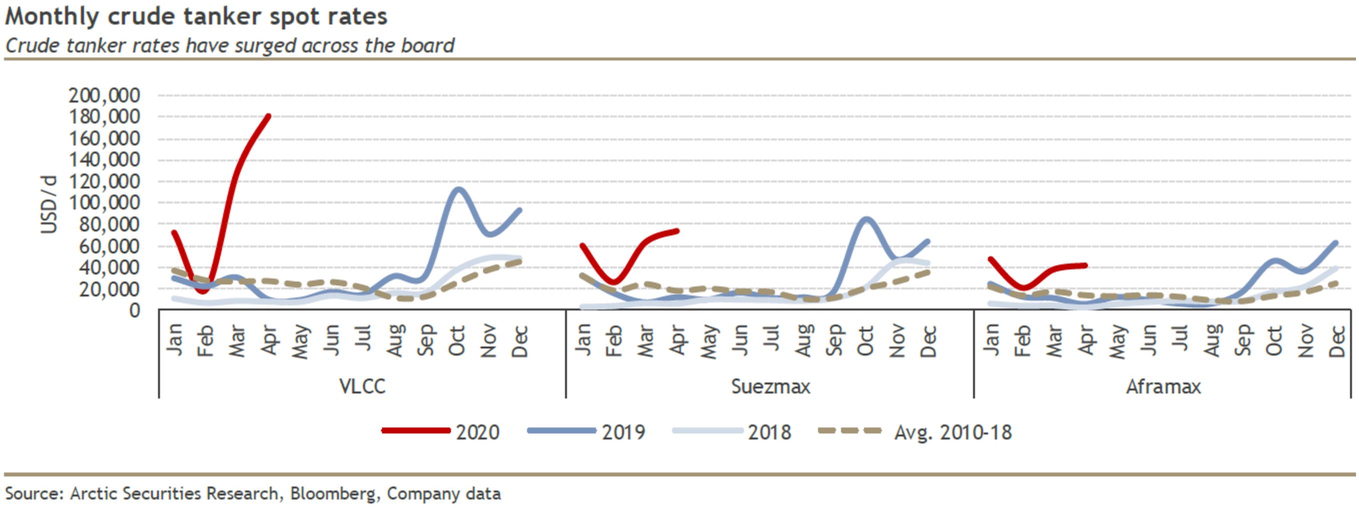
WTI Contango; Source: Big Picture Trading Chart Book, 7MAY20

Consequently, first quarter results for DHT, Euronav and Scorpio Tankers which already reported earnings were even better than anticipated. But share prices have recently corrected again, as the contango has flattened. The market obviously expects oil demand and supply to get into balance quickly, while not giving credit to the fantastic rate environment the sector has already enjoyed and is still enjoying, which has led to vastly strengthened balance sheets and growing dividend distributions.



Source: Arctic Securities, Shipping Sector Report, 24APR20

Euronav for example earned USD 1.01 per share, and is paying out USD 0.81 as cash dividend for 1Q 2020 alone, which at a current USD 9.70 share price represents a quarterly yield of 8.3%. And 2Q bookings suggest that results could again be in the same vicinity. In fact, most of these companies trade at 3 times or less this year's expected earnings, and record low EV/EBITDA levels, as share prices are obviously discounting a dramatic deterioration in the rate cycle.



Source: Arctic Shipping Sector Report, 24APR20

The exceptional current tanker rate environment can be seen above. To put this into perspective, let's look at the numbers: *"To simplify the math, VLCCs are up a shocking 625%, Suezmaxes are up 238%, and LRs are up 345%. Keep in mind that tankers have fixed opex, overhead, and financing costs of around $14-$20k/day depending on asset type and specific leverage, so the actual cash flows are up closer to 30x for VLCCs, 10x for Suezmaxes, and nearly 15x for LR2s.*

This means that a VLCC in this market can earn more cash flow in a single route for 60-80 days than in nearly five years of normal operations." – A case of exceptional value creation, indeed…

Tanker rates – Single voyages in US$ k/d

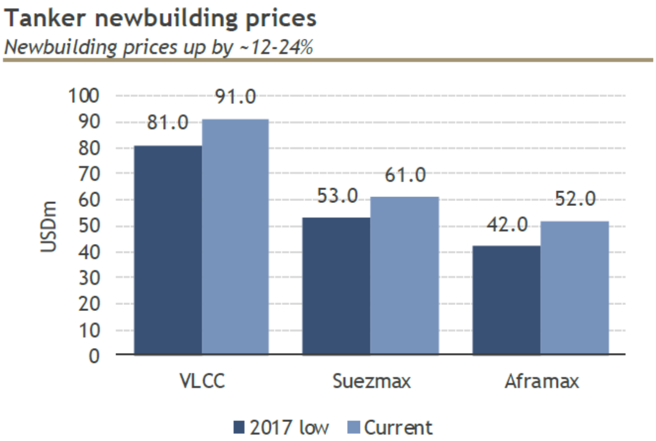
	2019 ytd	2020 ytd	Last week	This week
VLCC	25.6	103.8	175.4	185.7
Suezmax	22.1	59.5	69.0	74.8
Aframax	18.1	44.4	39.2	38.8
Pmax^	18.5	48.5	20.5	22.0
LR2	19.3	35.9	60.9	86.0
LR1	14.7	26.8	49.0	59.5
MR	14.7	22.2	22.1	26.1

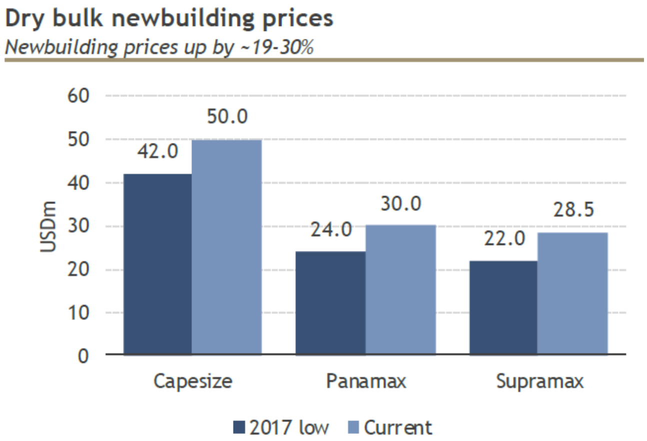
Source: Seeking Alpha, based on data from Clarksons Platou, 21APR2020

Admittedly, at the time of writing this, tanker rates have corrected already quite sharply, but are still generating tremendous free cashflows. And any such short-term corrections of the super-1Q-spike notwithstanding, analysts' see tanker estimates, both for 2020 and '21, overall as stable or improving. Together with strengthened balance sheets and cash distributions, current valuations hardly make sense, also in light of the low new order book.

I know there are many people who believe shipping has become an obsolete industry, and I tend to encounter pity rather than adoration for this kind of equity theme. And I do agree, this is clearly an old economy sector. But **IASF** has focused on bulk shipping and tankers, because dry bulk goods like iron ore, coal, grains, timber, etc., as well as crude oil, are usually not found where they are actually needed and consumed. And the only way to transport them is by bulkers and tankers, and I don't see anything that could change that in the near and distant future.

Well, I close this with one final observation on the shipping theme – even though there is of course always more detail one could add to make a proper investment case.





Source: Arctic Shipping Sector Report, 24APR20

I find the above chart quite interesting, as it shows that there is inflation as well in ship building. Hence, my argument for buying shipping companies that trade at significant discounts to book value / NAV, because their prices should be supported by rising replacement cost for their fleets. This should be particularly true if inflation makes a comeback.

Ok, finding myself on page 21 already, let's wrap this up, shall we? – Perhaps, I conclude this with a remark on gold and precious metals, which I have recently not mentioned a lot. I guess this is because the ongoing rally speaks for itself and vindicates our long-held bull case for both the metals and miners, a view which by the way is shared by a growing number of high-profile investors, the latest example being Paul Tudor Jones.

Source: [Hedgeye]

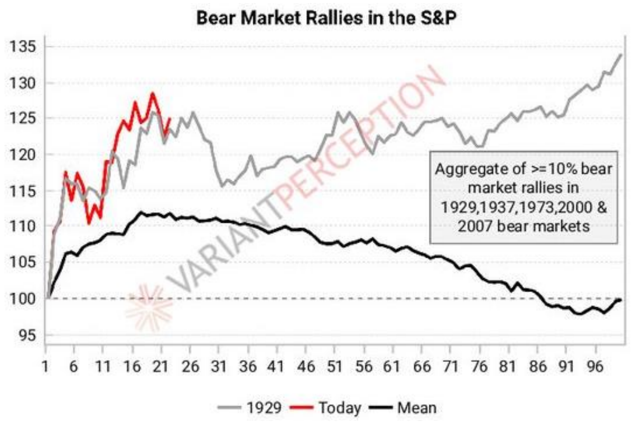
As responsible fund manager and co-investor in the fund, all my views expressed in this report, and particularly those concerning fund holdings must be considered biased and are not tailored to my readers' individual needs. Although I use great care in writing this commentary, it reflects my personal views and opinions only, and as all I do as a fund manager is subject to a great amount of uncertainty, you should not rely on it for accuracy. Thus, always consult a licensed investment professional if you are seeking investment advice! And remember that past performance is no guarantee for future results, and all investments involve risk including the loss of principal.

In Closing

The great Wayne Gretzky is quoted as having said: *"I skate to where the puck is going to be, not where it has been."* – This very much resonates with me on so many levels, as it has always been a core attitude towards my investment selection and allocation process. Sometimes, that meant I was too early, as those who have known me long enough will be able to confirm, but I would rather get the timing wrong than the actual investment case.

Today's investment environment is so distorted and manipulated on so many levels, that it is hard for me to even talk about markets anymore. (And do not let me get started on the bond markets, where economists are still willing to look for price signals and their meaning, completely ignoring the fact that there has been no market price in bonds for a decade.)

But this is the environment we have to face and work with. And considering that bonds, at least the traditionally safe categories, have become completely un-investable, we are stuck with exposure to cash, equities and alternative assets. Overall equity markets have bounced hard following the February / March crash, and history tells us that such a dead cat bounce is usually followed by more misery, as the hard economic realities reveal their full impact. - Will it be different this time?



Source: Variant Perception Research, @VrntPerception, [Twitter](), 23APR2020

Source: Markets Can't Ignore an Event This Extreme, Bloomberg's John Authors, 21APR2020

Personally, I doubt that. At best I would envisage something along the lines of the 1929 experience, but even that would suggest equity market weakness over the coming weeks and months. But we live in unprecedented times, and thus in a contrarian spirit have positioned our allocation in a way that should help us make money, even if broad equity markets continue to surf on the wave of central bank money, but is also likely to benefit from relative improvement / sector shifts.

In other words, we have chosen to build exposure to sectors that are now dwarfed in size by today's market darlings. I found it always a rewarding process to look for gems among the garbage rather than join the merry hunt for the current stock market's darlings, but it requires patience, discipline and conviction, which are core traits of any serious investor.

And at this point it only remains to thank my readers for their interest, my investors for their support, and to wish everyone good health and to stay safe in these challenging times.

Greetings from Schaan, Liechtenstein!

Best regards,

Hans

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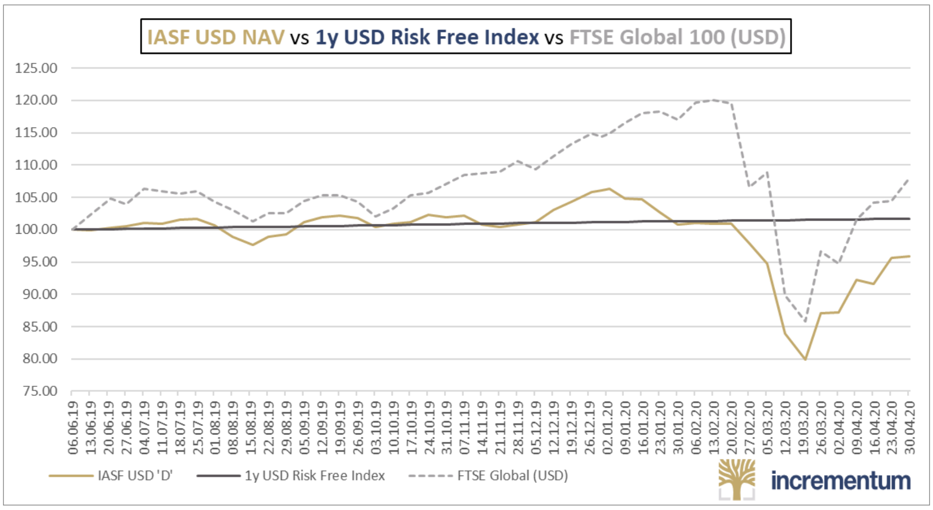
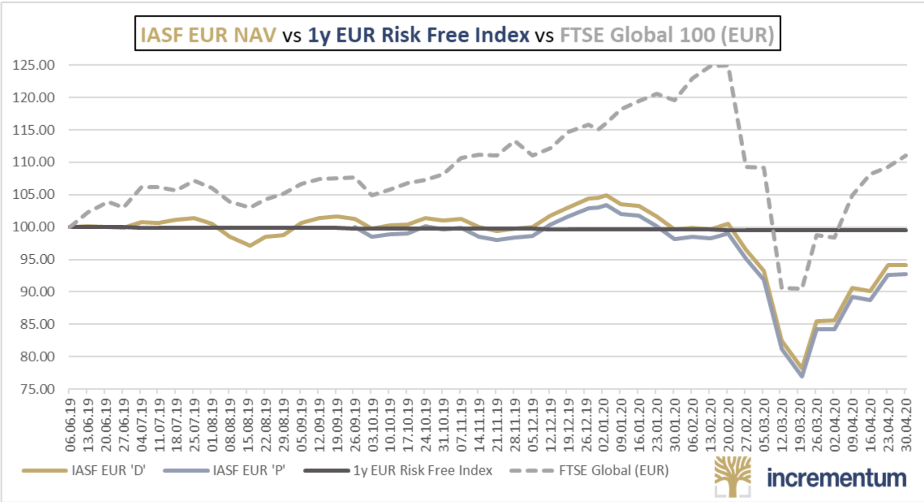
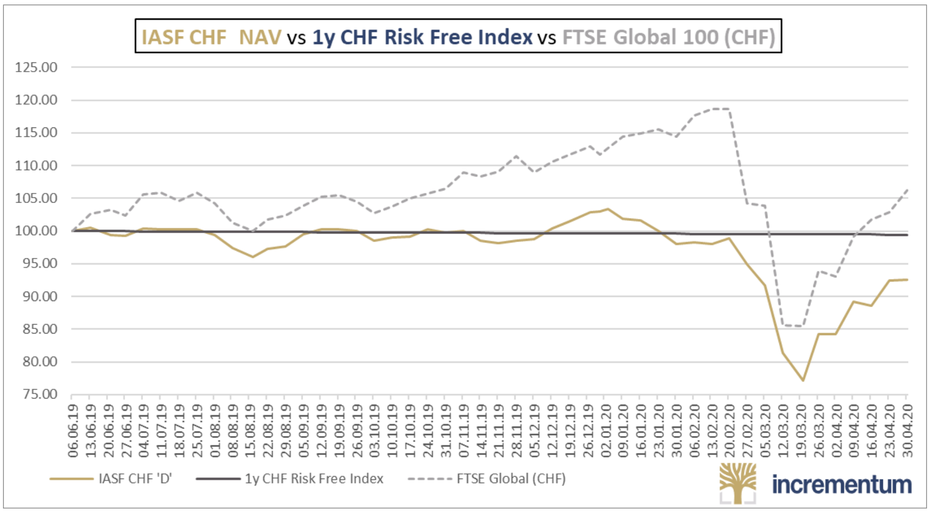
Appendix *







* Graphs display NAV of IASF 'D' shares as of last valuation date (**30Apr2020**), 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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