It´s All About Asset Allocation

June 2022, Newsletter#73

After having been falling for seven consecutive weeks, tied for the four-longest on record and narrowly avoiding bear market threshold, the S&P 500 finally started on May 20th the long awaited rebound: "Habemus Rally". With the index down as much as 18.7% on a closing basis, the question from here becomes whether the bad news is priced in or the decline has more moths to go. **Big picture, we can say that the market has discounted an economic slowdown but not a recession**. The timing and magnitude of any Fed pivot is the biggest factor in determining if the rally can continue deep into the second half of the year. Another hurdle for the market is that earnings estimates appear vulnerable to further downward revisions.

Financial markets are forward looking, so price-based (or technical) indicators are likely to be the first to signal the downtrend has turned into an uptrend. Typically, the market follows a four-step bottoming process: oversold, rally, retest, and breadth thrusts. We say "typically" because the changing structure of the stock market, with ETFs and algorithmic trading overtaking mutual funds and individual long-only investors, could have reduced the odds of a retest. In 2008 and 2020, for example, the market did not but the Fed was far friendlier than today. That's why, **we leave open the possibility of the market skipping step three.**

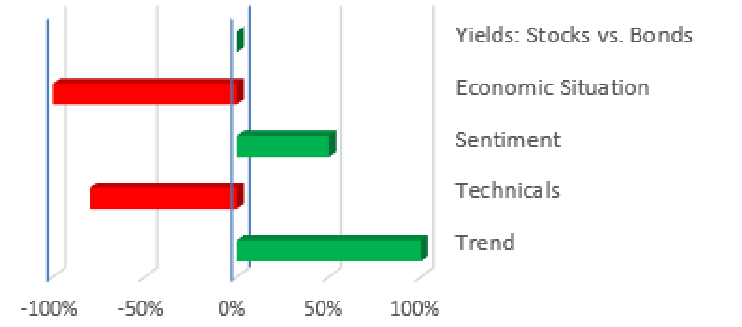
The recent rebound has been remarkable but has not triggered enough breadth thrust signals to give the "all clear" signal. For assurance that we're not seeing a repeat of March, when those indicators proved to be premature and were stopped out, **confirmation will be needed**. For the breadth to improve, participation will be required across the ACWI sectors, including renewed strength in the Information Technology and Consumer Discretionary sectors. Both have underperformed for most of the year, a negative influence on the ACWI given their respective weights of 21% and 11% in the index. The recent gains have been encouraging but it remains to be seen if their rebounds are the start of sustained recoveries or part of a March replay – short-lived bounces to be followed by the resumption of the longer-term downtrends.

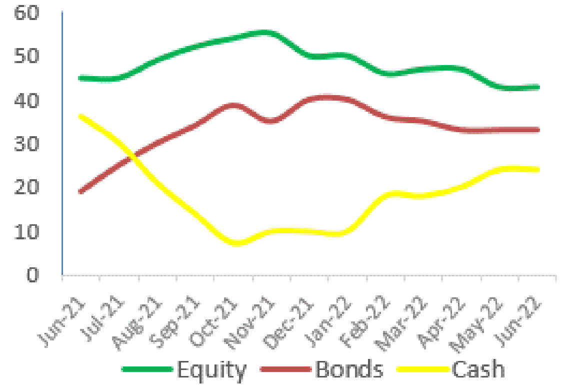
Our Global Flexible Fund, fLAB Core H-USD, has achieved to close this volatile month nearly flat (-0.13%), thus performing -7.13% YTD.

For June, our Asset Allocation model remains unchanged: 43% stocks, 33% bonds and 24% in cash. As mentioned before, so far, it's a bounce from deeply oversold conditions. We need a clear improvement from our fusion analysis indicators to trust it.

fLAB Core Asset Allocation Model		Jun-22	Benchmark
	Stocks	43%	55%
	Bonds	33%	35%
	Cash	24%	10%

Equity vs. Bonds Relative Strenght by Betalphing 5 Indicators





red (bond & cash preference) green (equity preference)

Equity Regional Allocation vs MSCI World AC			
Europe Ex-UK, Canada	*OW*	*USA*	*UW*

Benchmark (US 57%, Eur 13.4%, Emerg Mk 12%, Jap 7.1%, UK 4.3%, Pacific 3.3%, Can 2.9%)

Equity World Sector Allocation			
Cons Staples, Energy, Materials, Health Care & Utilities	*OW*	*Cons Discretionary, Comm Services & Technology*	*UW*

Government Bond Allocation vs Barclays Global Government Bond Index			
Europe	*OW*	*US*	*UW*

Benchmark (US 48%, Europe 25%, Japan 21%, UK 6%)

The S&P 500 rebounded strongly in the back-half of May and eked out positive in the month, while the Nasdaq could not. The overall MSCI ACWI (local currency) performed slightly negative in May (-0.23%) weighed down by the US since the major regions composing the index closed on positive territory. Value outperformed Growth, again, but leadership was volatile during the month. Cyclical Growth sectors, like Consumer Discretionary, Technology, and Communication Services, which led the selloff, have been among the best performers since May 20. Likewise, with the defensive sectors it has happened the opposite. These leadership shifts are not uncommon during a bottoming process. **Our sector model continues to favor Value over Growth sectors, but to a lesser degree than recent months**. If evidence builds that a sustainable uptrend is underway, we will adjust our sector allocation which is working so well this year. The same can be said about our geographical bets.

Global Government bonds posted losses once more, with some divergences. After reaching 3.12% on May 6th, the US 10-Year Treasury yield receded while the 10-year German Bund climbed to new highs as the markets are now pricing in a rapid pivot by ECB. In fact, in today´s meeting, t**he markets await Lagarde to announce that they plan to raise rates in July. That could set up a "sell the rumor, buy the news" situation** . Most investors expect a 25 bp hike in July, although there has been talk of a 50 bp increase. Markets are pricing further increases in 2023 with yields peaking below 2.00%. That might be too high if inflation settles down. Another divergence that caught our attention is that inflation expectations (5-year/5-year swap rate) have not confirmed the new highs in bund yields. We will be monitoring all that. For the time being, we continue underweighted in terms of duration (2.43 for the overall fund). In terms of currency, the US Dollar slid (-1.79% against the euro) as traders have adjusted Fed rate hike views, more hawkish ECB comments and the appetite for risk returned. We keep a 20% real dollar exposure which we will continue to manage tactically.

Our Relative Return Fund, fLAB Satellite H-USD, continues positive in this difficult year: +0.22% YTD.

The compartment is investing 50% in a low risk, low duration diversified fixed income portfolio plus 26% in some uncorrelated and tactical positions, being the rest in cash. We have not changed our allocation in such a volatile month. In terms of performance, global commodities (3.48%) and the equity multiestrategy position (16%) have contributed positively while the core bond portfolio, dollar exposure (15%) and gold (weighting 3.6%) have detracted some profitability. Stock and bond downtrends this year, produced extreme pessimism readings that have started to reverse on an increased recognition that inflation may have peaked. The equity rebound has thus been more decisive, with the Barclays Global Aggregate now testing its May low. We will remain flexible in terms of equity exposure and duration (1.78 for the overall compartment), always committed with our low volatility target. **fLAB Satellite USD Clean Share Class, has just been rated 4-star by Morningstar for the last 3 year period, so you may consider to add this strategy to your more conservative or uncorrelated portfolios.**

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