Capicura Partners – Outlook 4th Quarter 2021

The art of ignoring the noise

- ***Monetary policy tailwind is fading – but financial markets still supported by a gentle breeze***
- ***China Evergrande is not a Lehman Moment, but still a reason to be critical towards Chinese investments***
- ***Inflation not only transitory – supply chain issues lead to elevated prices mid-term***
- ***Negative real interest rates bode well for real assets – equities remain favoured asset class***

It is with great pleasure that we send you our first quarterly Capicura Partners Outlook. We have always tried to keep our outlooks short and sweet, highlighting the most current events, emphasizing sustainable trends and ultimately trying to define an asset allocation for the next quarter and beyond. While we have changed the format somewhat, we continue to hope that this regular update is a helpful guide in today's financial markets.

We are very grateful for any input or feedback you may have both on format and content – ultimately, this is a publication which should be interesting and enjoyable to read. Also, we sincerely hope that our quarterly update creates discussion points leading to specific investment ideas.

«There are always enough reasons to worry»

September and October are often months during which sentiment changes and investors become more risk averse. After the last 18 months of upbeat markets in various real assets, it is quite understandable that investors are seeking to take some chips off the table. In this nervous period, it clearly does not help that China's largest and massively indebted (>USD 300bn) property developer, Evergrande Group is on the brink of bankruptcy. With the property market representing roughly 30% (direct and indirect) of the Chinese economy, we strongly believe that it is in China's best interest to conduct an orderly wind-down (debt restructuring) of Evergrande. So, our base case is that a «Lehman Moment» can be avoided. Still, due to the importance of the property sector, such a crisis will clearly affect China's growth and subsequently reduce global growth expectations. An additional headache is the risk of a shutdown of parts of the US government. If the debt ceiling cannot be agreed upon by October 1st, we will again experience a "US Shutdown" with some government personnel being asked to stay at home. We have seen this quarrel many times in the past and based on history, we expect a solution to be found. The picture is somewhat less clear in Germany where last weekend's "Bundestagswahlen" did not bring forward a clear winner. Various coalition combinations are thinkable and while the outcome is still uncertain, it seems fair to assume that a dreaded left-wing government is not in the cards. This should provide some comfort to financial markets. But the biggest challenge ahead is by far the fear of rising inflation and the expected end to tapering by the FED (ca. mid 2022) which should be followed by first interest rate hikes (earliest end of 2022). We fear that the recent pick-up in inflation is not only transitory as supply side constraints are keeping prices elevated in many sectors. But short-term, central banks are not moving on tapering and are far away from raising interest rates any time soon. So, interest rates will not rise markedly for quite a while or rather, they are not allowed to rise due to the vast public debt around the globe. This ultimately leads to negative real interest rates (see Fig. 1) forcing investors into even more risk.

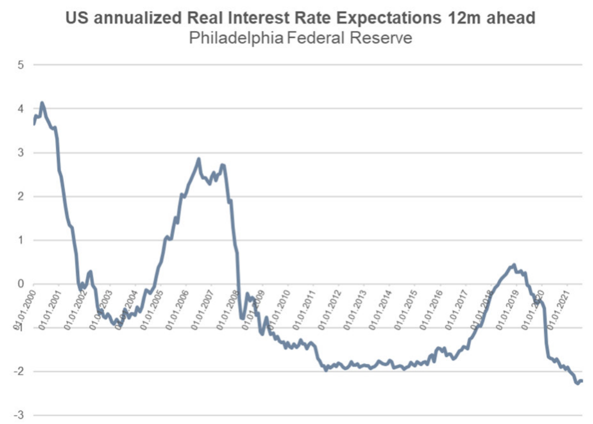

***Fig. 1)** Data Bloomberg / Chart Capicura Partners*

«Global PMI data points towards further expansion in USA and Eurozone”

While PMI data shows a slowdown in economic activity, the numbers still indicate expansion. This, especially in the Eurozone and in the USA. Many Asian economies have started to contract with the Evergrande crisis and its knock-on effects being the main reasons.

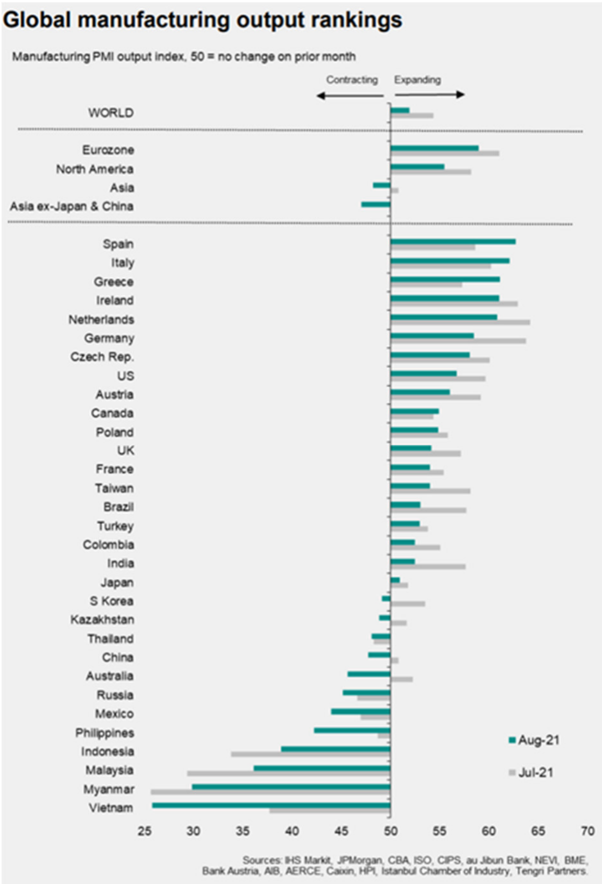

Fig. 2) *Source: IHS Markit*

«Market participants to become more selective»

After a good year for financial markets and for equities in particular, the coming quarter(s) will require a more selective approach in regard to sectors, style and regions. An active manager should be able to outperform a passive strategy (index product) in such an environment. But the biggest driver of real assets going forward will be negative real interest rates, solid economic growth and ample liquidity still provided by the central banks.

«Sceptical investors are good news for equities»

From an investor sentiment and contrarian’s point of view, equities look well underpinned. The CNN Fear&Greed Index (Fig.3) is currently at its lowest level for the year. Additionally, technical market analysis also supports a continuation of the rally in real assets.

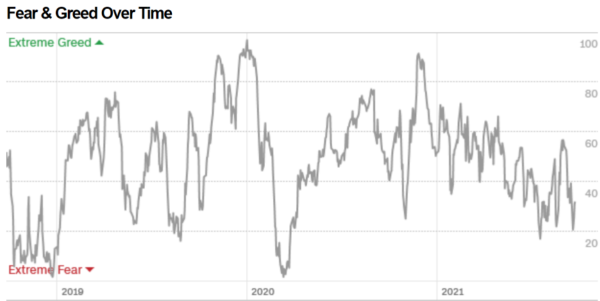

Fig. 3) *Source: CNN Fear&Greed Index*

«Despite increased noise, stick to a constructive asset allocation »

Based on above and despite the increased noise, we remain convinced that investors should hold a substantial portion of their portfolio in real assets and especially in equities. Clearly, any asset allocation should take the individual risk appetite into account and ensure that the overall comfort level is found. Investors in cash and nominal values will get hurt in a negative real interest rate environment and will hence not be rewarded for the risk taken.

Asset Allocation	
Cash	10%
Fixed Income	20%
Equities	60%
Alternative Investments	10%

Fig. 4) *Suggested asset allocation for a Balanced Portfolio in Q4 2021*