Haven Global Partners, LLC
Market Outlook: April 2022

Stock Picking is Back!

For several years now investors have been conditioned to stay committed to being long global stocks. Stock prices have moved pretty steadily higher during this time. The gains investors have made in stocks lately have been fueled by a combination of easy monetary policy from the Federal Reserve, the European Central Bank and several other leading central banks as well as generous handouts granted by governments from Brasilia to Washington and of course booming corporate earnings. It has made sense for investors to be long stocks because of a perceived desire on the part of central banks, especially the US Federal Reserve to support stock markets (sometimes known as the Fed put). For these reasons investors have taken to putting more money into stocks, sometimes aggressively, any time the stock market falls. This so-called buy-the-dip strategy has rewarded buyers. There is reason to suspect that may no longer be the case, though. Earnings should still be relatively solid this year, but the cash has stopped flowing out of Washington and the Fed has begun raising interest rates, while pledging to stop buying bonds. This should serve as a warning for the buy-the-dip crowd.

The interest rates on US Treasuries have moved dramatically higher. During the first quarter of this year, the US 10-year yield rose from 1.5% in January to almost 3% now. Higher interest rates on Treasury bonds denominated in the world's reserve currency and carrying the full faith and credit of the world's one remaining superpower are the quintessential example of a risk-free investment. And more attractive risk-free investments will act as a counterweight to the belief that investing in stocks is the only thing that makes sense.

There are more things for investors to fret about. US stocks had their worst January since 2008. Tech stocks did even worse than that! For tech investors who aren't likely to be getting any dividends, rising interest rates represent a real threat. The future earnings that they are waiting to receive are minimized in an environment where interest rates are going up. So, an aggressive, hawkish Fed facing much higher, more persistent and broader based inflation will only lead to even higher interest rates going forward. This may lead to a scenario where too much is being asked of earnings, as they are the only positive for stockholders to hang on to.

In last quarter's Outlook we predicted higher volatility and higher volatility has been visited upon us. By whatever measure you prefer, things in the capital markets have gotten spicier. Stock market participants' favorite volatility measure is the CBOE's Volatility Index, known as the VIX or the fear index. This has moved steadily higher since making its post-COVID bottom in June of last year.

An increase in volatility is best met by a measured, dispassionate response, not a knee-jerk reaction such as buy-the-dip. Compiling a list of quality stocks and identifying a price at which one might like to own them is sensible. Finding companies with the strongest competitive positions, best operations and greatest capital

allocation opportunities that are managed by skilled, savvy capital allocators with proven records of shareholder value creation is critical to maximizing the opportunities which may soon be presenting themselves. This suggests that experienced, disciplined, fundamental stock pickers will have a tremendous advantage in these markets. The key is not to worry about what the stock market might do, rather focus on what you need to do in the stock market. Identifying companies that tend to do best when financial conditions are tightening requires a focus on Quality. That has always been our approach. At this particular point in the cycle given current events and the increase in volatility, we believe there is a strong case to be made that fundamental-based stock picking can outperform going forward.

War broke out in Eastern Europe, adding to the list of worries global investors must address and serving as still another contributing factor to the world's inflation problem as the prospect of an OPEC+ nation at war drove oil prices higher.

In the meantime, we still have to talk about China. China was front and center during the quarter, hosting the Winter Olympics. They are in negotiations between the US & Russia as to who they will side with during the war in Ukraine. There will be an election in China later this year and the Chinese Communist Party have some plans they wish to promote. There are five themes China will follow to try and win the future:

1) Self-sufficiency: Beijing desperately wants to win and control certain fields. They will put policy support behind fields such as wireless technology & semiconductors
2) Upgrading Manufacturing capability: Robotics will be key to them.
3) Healthy lifestyle: an increasingly affluent middle class has aspirations, which will drive demand for healthier products and health care services
4) Renewable Energy: China hopes to dominate solar
5) Financial Market reform: expect a continuation of the ongoing liberalization of China's capital markets

There have been questions raised as to whether investing in China made sense at all. China is one third of the Emerging Markets indices, you need to invest there if you are serious about EM investing. But in order to invest there successfully, you have to consider aligning your investments with the things the government (CCP) wants to accomplish. Keep a close eye on any companies which can help China accomplish things on that list.

As a final thought, keep in mind there is a re-opening trade still out there somewhere because the actual end of the COVID pandemic, whenever it comes, will feel like a boom.