ECOGNOSIS ADVISORY LTD

From the Greek: ΟΙΚΟΝΟΜΙΚΗ ΓΝΩΣΙΣ (Ekonomiki Gnosis, Knowledge of Economics). Ecognosis is a global financial, economic advisory and information service, covering economic and financial developments, equities, fixed income, forex, commodities and other assets. Econotes is a research publication available free on our internet site and to the public in Hong Kong. It is not a solicitation for business and neither does it contain investment suggestions on specific and named securities including any buy, sell or hold advice. It is written by Dr. Andrew F. Freris based on 54 years of market experience which includes senior positions with GT Capital, Salomon Brothers, Bank of America and BNP Paribas as well as senior academic posts with universities in London and in Hong Kong

Level 20, One International Finance Centre, 1 Harbour View Street,, Central, Hong Kong. Tel: 852 3167 4591, Mob 852 9738 0944, Email: afreris@ecognosisadvisory.com, Website: www.ecognosisadvisory.com, FB: @ecognosis

ECONOTE No. 107 "It ain't over till the fat lady sings: Investment suggestions in a Covid and Crashing world. 4/7/2022

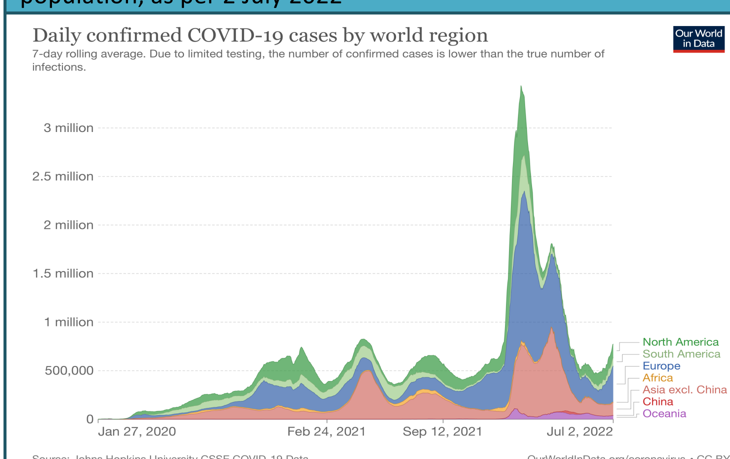
Summary	**Investment Conclusions**
The on-going crash of the markets has distracted from the "boom" taking place in Covid infections and which peaked, but did not then decline during Dec.2021 to February 2022.The lifting of domestic and travel restrictions in most countries (bar China and Hong Kong) has led to information gaps as infections, hospitalization and death numbers have been more difficult to collect and, hence, to disseminate. Nonetheless the infection is "alive, kicking and growing " (poor choice of words here!). The fact that it does not make headlines does not make it any less damaging to the economies, than the Fed hikes which dominate the news. We outline here the current Covid trends without, of course, making any epidemiological forecasts which are outside our field .We connect these trends with the on-going market crash making some investment suggestions which are not "recovery plays" or connected with the timing of Fed ending hiking.	The main precept of this report is that markets are not paying enough attention to Covid's trends of infection. The lifting of restrictions in nearly all-major and minor countries, bar HK and China, has removed Covid statistics from headlines. The astronomically high surge of infections in early 2022 shows that the pandemic is very active could disrupt again the global economy. Basing investment strategies on the trajectory of the US Fed focuses only on one factor affecting asset prices. The other factor, Covid infection, is unforecastable and the way to deal with its potential impact on economies is, possibly, the following. Pay less attention to "recovery plays" after the Fed hikes are over, but to investment opportunities, which are unconnected, for now, with the cycle and are driven by specific events or stories.

Opera, terminal events and forecasting the end

"It ain't over till the fat lady sings" is a colloquialism meaning that one should not presume the outcome of an event still in progress. The phrase can also be used when a situation is nearing its end.The homily is attributed to Dan Cook, a Texan sports writer, possibly with reference to the popular view of (politically incorrect !) sizeable sopranos singing the dying aria at the end of the opera.Here it simply means that the progressive disappearance of Covid headlines from the media ,as most counries lifted Covid restrictions, does not mean that the pandemic is fading and the only thing we need to worry is the Fed and rate hikes.Consider the following points.**First,** Covid has caused enormous economic damage through its disruption of production and consumption, the infamous supply bottlenecks.Covid impacted the labour force but , far more damaging,the policy actions of governments (lock downs, social distancing, travel restrictions etc) in trying to limit the spread of the infection multiplied that damage.**Second,** in order to ameliorate this "double damage", governments loosened massively their fiscal and monetary policies.This came after the extensive monetary ease following the 2008-9 financial crash.**Third,** the accumulation of funding which led to a prolongation of the zero interest rates, led to extensive asset price inflation but not CPI inflation.This was reversed by the outbreak of the Ukraine war at the start of 2022. The nascent recovery in most of the major economies was now combined with extremely sharp rises in the prices of oil, gas and commodities, especially food, caused by the sanctions on Russia and by the physical effects of the war on shipping and transport.**Fourth** ,and last, the world economy finds itself hemmed by restrictive monetary policies mainly in the US and EU, but not from Japan or China, and by rising CPI .

However,the urgency of CPI inflation is by no means the same in all countries, the reluctance of most economies to follow the US rate hikes is shown in the weakening of all forex rates versus the USD.(See Fig.3) On top of this, as Fig.1 shows, infections are rising again, after the tsunami of Dec.2021-Feb.2022 (Fig. 1).The spread of vaccination (Fig. 2) is unable to contain infections because of the mutation of the virus. There are news of common flu also spreading thus aggravating the situation.Countries are beginning to think again about their past restricitve policies while China and HK stay with their zero targets.

Fig 1. Seven day rolling average of infections per million of population, as per 2 July 2022

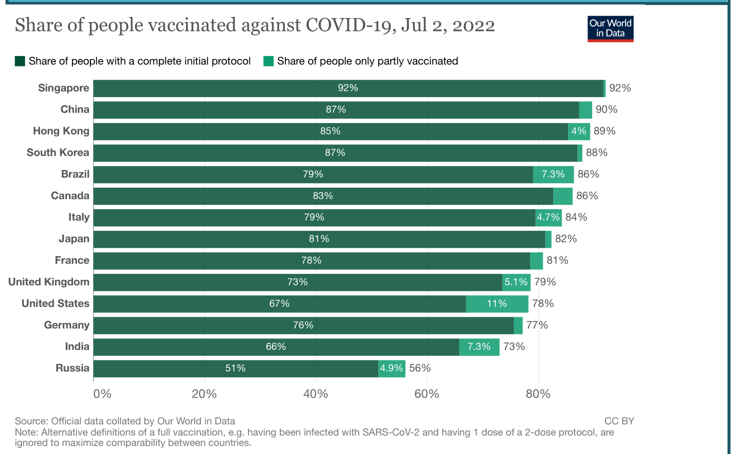


Source: Our World in Data (OWD)

Why worry about the nature?

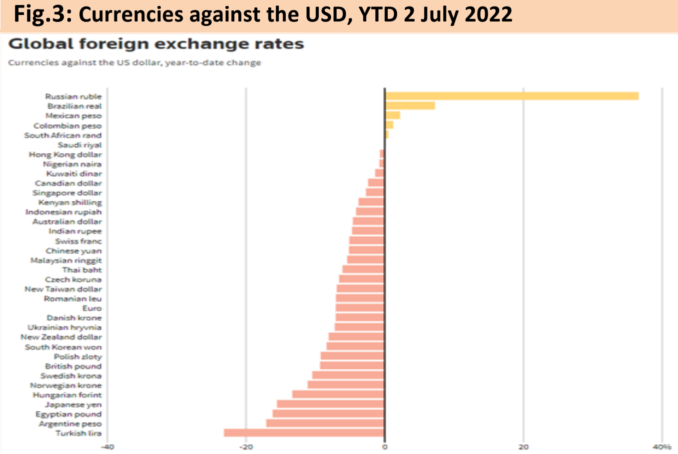
The message sent out above is that the current (May-June) market crash is the outcome of a perfect storm, which had in its middle the Covid pandemic. A lot of the economic damage was man-made, that is lock-downs, travel restrictions etc as opposed to Covid impacting the labor force. If Covid was to resurge, as it did at the start of the year, and if this time, unlike the Omicron mutation, the infection is not "benign", concerns over the Fed hiking would fade in the background, as surging infections rates could force a policy rethink. This is not "gloom and doom armchair forecasting" as six month ago the virus showed what it could do in terms of spreading. So the "fat lady has not yet sang ". Nature may not be controllable but investment policies taking into account this uncontrollability are available, and some samples are shown here. What we can do is devise investment solutions and suggestions, which do not rely on financial forecasting, such as the end of the Fed hikes and the cyclical recovery, while keeping in the background the potential Covid interruptions.

Fig.2: The spread of vaccination as percent of population



Source:OWD

Fig.3: Currencies against the USD, YTD 2 July 2022



Source: Reuters

Forecasting the end of high rates and basing a full strategy on that alone is irrelevant when Covid can change the scenery overnight. And this brings us to the war in Ukraine, which continues to add unforecastable uncertainty, as clearly this is a war, which may take months if not years to resolve.

Hence our approach on investment suggestion is based on "stories" which are not related to the ending of Fed hikes or early ending of the war or imminent Covid resurgence. Subject to the HK compliance regime within which Ecognosis works, consider the following "stories". **Defence stocks.** The war in Ukraine has led to a complete restructuring of NATO plus multibillion arms aid from, mostly US, and UK to Ukraine, materiel which will need to be replaced. Germany, for the first time in the postwar period, will fully rearm. In Asia, where there are various areas of frontier conflict, some of which had led in the past to actual wars and armed conflict, there has been a resurgence of actual and planned spending on defence. Countries involved include India, Taiwan, S.Korea and Singapore. Further out, Australia is extending its blue water navy. The major defence contractors are primarily US and EU corporates, but they are a few investable Asians. The surge in defence spending will not be a "one-off" as defence commitments are long term and are spread over several years.

Concluding with the investment stories

China has a large defence industry but, for obvious reasons, not easily accessible if at all. Under the umbrella of defence stocks, we can add electronics and chips makers dedicated to defence, not just on electronic warfare but also on drone technology. **LNG both producers and shippers.** It has become clear that the Covid disruption, and more specifically the Ukraine war, has distracted attention from the Climate and Emission targets of the Paris agreements. The shortages of gas has led to a return to coal production of electricity, to the strong protest as what this would do to the progress made so far on CO^2 emissions. LNG offers a half way solution, as its CO^2 emissions are about 50.0% lower than those of coal. Hence LNG will continue to be substituted where possible for coal subject, of course, to the speed of conversion of the power plants. There are significant shortages in the global shipping capacity and distribution of LNG, as it requires special facilities at ports to be discharged and distributed. Companies related to LNG should do well not just now by also in the near future. **Pharmaceuticals.** The sector was equally hit with all other sectors in the recent equities fall. This is not a miracle sector, but sector which will be kept busy not only with vaccines, which not all pharmas do, but also potential treatments of the "long Covid" the debilitating after-effect of Covid lasting, potentially for years, and not just weeks.

Lastly, an odd sounding investment proposal. I confess that I, too, got sucked in with the rush to suggest **assets, which did well in inflation times**, such as (of course!) property. Markets have crashed as they are convinced that the Fed will hike long and hard till US inflation is brought down, possibly to the 2.0% level. If that happens, then there is absolutely no point in putting money now into assets, which might benefit if inflation is not only historically high, but also stays high and possibly continues to accelerate. None of this forms part of Fed's expectations! Inflation should fall quickly under the hammer blows of 50 bps hikes, and then stay low as the monetary expansion of 2008-9 is withdrawn from the system. A similar, but far less aggressive scenario, can be laid out for the ECB. Conclusion? Consider unwinding these inflation proof investments unless there are serious reasons to believe that the Fed will fail in its task and inflation will stay high.