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**Bulltick Research and Strategy**

Kathryn Rooney Vera
Head of Research & Strategy
krooney@bulltick.com
+1 786.871.3758

Gregan Anderson, CFA
Macroeconomic Strategist
ganderson@bulltick.com
+1 786.871.374

# Global Cross Asset Strategy:

## Inverted Yield Curve and a Tightening Fed

The 2-30 yield curve spread briefly turned negative last week, and currently stands in the low single-digits, a clear indicator that market participants are bracing for headwinds to economic growth and market performance. Inflation and slowing economic growth pose risks for the US economy as a more hawkish, woefully behind-the-curve (as Bulltick Research has contended for the past year) Fed launches a more aggressive 50bps hiking cycle.


While such a scenario should not be discounted (and indeed it is an alarm that Bulltick has been ringing for some time now), we should also bear in mind that nominal pricing of companies should benefit from higher prices, as companies are able to pass along higher costs and earn higher profits, at least in nominal terms. This should in theory be especially true amid a tight labor market and solid (again, nominal) wage gains.

| Asset | Spot | Chg In Past 2 Weeks | YTD Change | End- 2022 Target |
|---|---|---|---|---|
| USG10Y | 2.60 | +31bps | +109bps | 2.75 |
| USG30Y | 2.62 | +14bps | +72bps | 3.25 |
| JGB10Y | 0.25 | +2bps | +17bps | 0.10 |
| DXY | 99.61 | 1.00% | 4.11% | 98.00 |
| EUR | 1.09 | -0.94% | -4.12% | 1.18 |
| JPY | 123.79 | -2.14% | -7.04% | 115.00 |
| MXN | 20.15 | 0.37% | 1.89% | 22.00 |
| BRL | 4.71 | 2.42% | 18.23% | 5.20 |
| SPX | 4487 | 0.69% | -5.85% | 4700 |
| IBOV | 118026 | 0.48% | 12.60% | 120000 |
| MEXBOL | 55467 | 0.57% | 4.12% | 56000 |
| Brazil 10Y | 11.48 | -64bps | +69bps | 11.75 |
| Mexico 10Y | 8.54 | +14bps | +98bps | 7.90 |
| MXEF | 1157 | 1.41% | -6.11% | 1450 |
| Gold | 1926 | -0.93% | 5.28% | 1950 |
| WTI Crude | 97.1 | -15.51% | 29.12% | 110.0 |

*As of 04/06/2022*

While such a scenario should not be discounted (and indeed it is an alarm that Bulltick has been ringing for some time now), we should also bear in mind that nominal pricing of companies should benefit from higher prices, as companies are able to pass along higher costs and earn higher profits, at least in nominal terms. This should in theory be especially true amid a tight labor market and solid (again, nominal) wage gains.

We have updated many of our forecasts given the change in the macro picture from Russia's invasion and the ensuing disruption in food and energy prices. We see the UST 10 year at 2.75% (from a prior 2022 year-end forecast of 2.25%), WTI oil at $110 p/b, SPX base case 4,700, fed funds ending at 2.00%, US economic growth of 2.8% and core PCE inflation at 4.5% y/y.

Fixed Income.....3
Forex.....5
Equities.....7
Alternatives.....9

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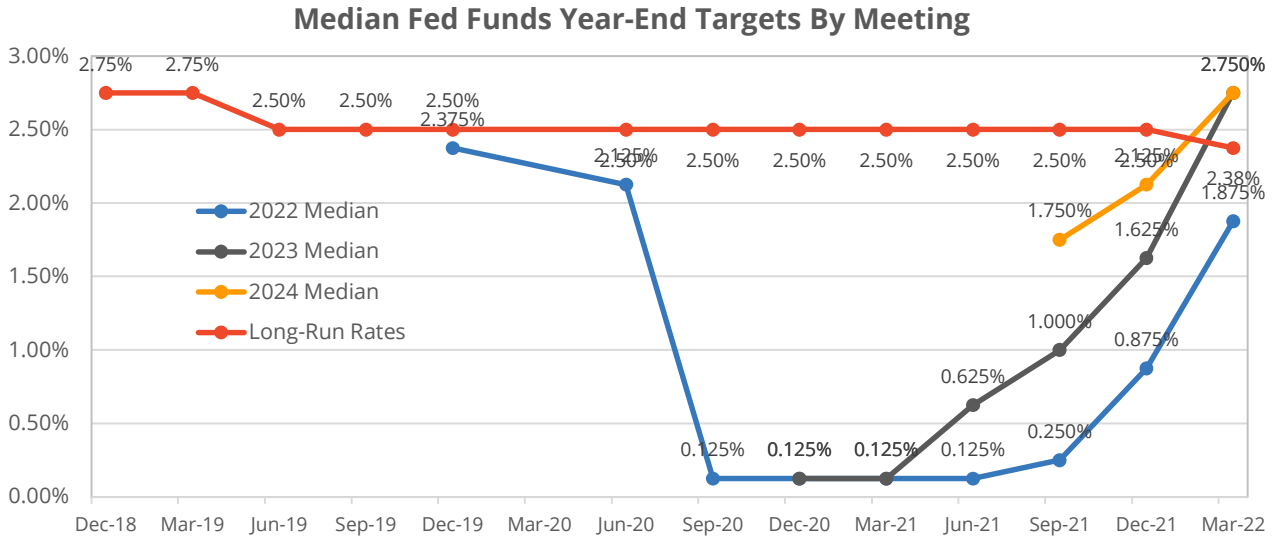
The Fed has taken a far more aggressive tone, and according to the median 'DOTS Plot' estimate of the Fed funds trajectory, fully expects to follow up with hawkish action. The latest plot envisions a full percentage point more of rate hikes, a reflection that the Fed has realized that it is behind the curve and must work diligently to anchor inflation. While many are concerned that an aggressive Fed could put the brakes on growth, we view it as on-balance positive that officials are taking the inflation problem more seriously. We maintain our exposure to risk assets and note that in an exceptionally high-price environment, solid companies with the ability to pass on costs will likely outperform traditional safe-havens like USTs, given the prospect of declining bond prices amid the hiking cycle.




*Source: Bloomberg, Bulltick*

# Fixed Income Strategy:

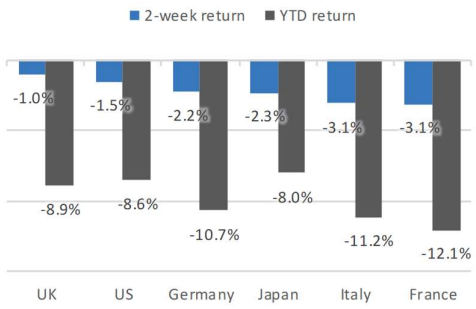
- ***Recent Fed commentary, the DOTS plot, and official action all point to a more hawkish orientation*** on the part of policymakers, as the Fed comes to terms with the fact that it is well behind the curve on curbing price growth. Futures markets are pricing in over 200bps of *additional* rate hikes before the end of the year, including a high probability of multiple 50bps hikes. This month's jobs report, which saw unemployment fall even lower to 3.6%, allows Fed officials to focus on only one prong of their dual mandate, that of inflation.

- ***While we believe that the Fed will ease on its hiking cycle once inflation peaks and begins a downtrend, we nonetheless concur that the landscape has changed***, as has the Fed's attention to it. We have increased our forecast for both the Fed fund's rate (to 2.00% by end-2022), and for US treasuries (we now are expected 3.00% for the 10Y treasury by end-2022, up from 2.25 previously).

- ***Apart from Fed action on rates, investors will pay increasing attention to the roll-off of the balance sheet,*** which at over USD9trn is nearly double what it was prior to the global COVID pandemic. As such, we expect that the Fed will need to embark on a more aggressive roll-off than they did in 2017, on the order of USD100bn/month (versus USD50bn/month in 2017).

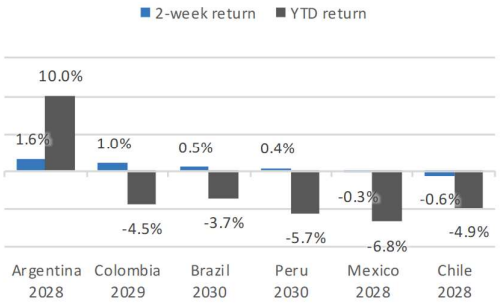
- ***To ensure that mortgage-backed securities do not become a much larger portion of the overall holdings, MBS selling will accelerate*** at an even faster relative pace, such that we expect that mortgage rates will rise more quickly than USTs, producing headwinds for the red-hot housing market, which we expect to cool off.

**Developed Markets 10Y Total Returns**




**EM Local Currency Bond Total Returns**


**EM USD-Denominated Bond Total Returns**

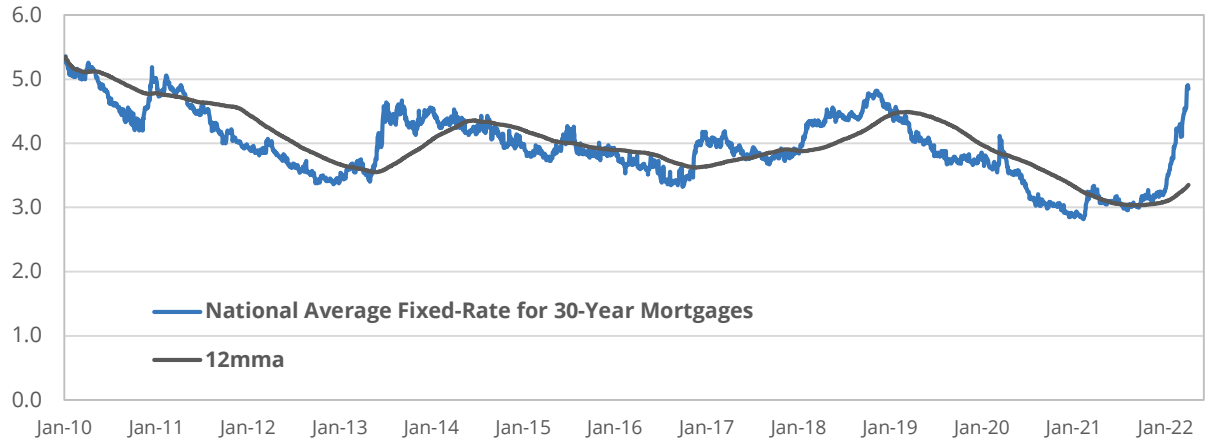



| Benchmark Asset | Begin-2022 YTM | Current YTM | YTD Interest Gains, % | YTD Capital Gains, % | YTD Forex Gains, % | Total YTD Return, % | 2022 Target YTM | 2022 Return, % |
|---|---|---|---|---|---|---|---|---|
| UST 10Y | 1.51 | 2.56 | 0.37% | -8.92% | - | -8.56% | 2.25 | -5.16% |
| German 10Y | -0.18 | 0.58 | 0.00% | -6.88% | -4.12% | -10.72% | -0.20 | 4.02% |
| Japan 10Y | 0.07 | 0.20 | 0.03% | -1.30% | -6.86% | -8.04% | 0.10 | -0.14% |
| Mexico MBONO 2031 | 7.56 | 8.44 | 2.02% | -5.61% | 2.73% | -0.96% | 7.90 | -1.71% |
| Mexico USD, 2031 | 2.95 | 3.93 | 0.72% | -7.49% | - | -6.77% | 3.10 | 1.48% |
| Brazil BRL 2031 | 10.84 | 11.41 | 2.76% | -0.35% | 19.55% | 22.43% | 11.75 | 17.14% |
| Colombia TES 2031 | 6.34 | 9.23 | 1.85% | -17.34% | 9.95% | -7.08% | 8.00 | 1.37% |
| Chile CLP 2032 | 5.65 | 6.06 | 1.53% | -1.43% | 8.38% | 8.49% | 6.00 | 9.33% |
| Argentina ARS, 2026 | 49.55 | 49.63 | 9.59% | 11.95% | -7.22% | 12.77% | 50.00 | -6.05% |
| Peru Soberano 2031 | 5.90 | 6.87 | 1.70% | -6.46% | 8.25% | 3.10% | 6.00 | 8.54% |

*Source: Bloomberg, Bulltick. All returns are in USD* *As of 04/05/2022*

Average fixed-rate mortgages nationwide are now hovering around 5.00%, the highest they've been since 2011. An inventory shortage, a backlog of demand, and a construction sector playing catch-up, and a historically low proportion of current mortgages with adjustable rates will all preclude a collapse in the housing sector, despite these pronounced headwinds. Nevertheless, we expect mortgage rates to continue to rise, and believe that further upside to real estate will be limited.

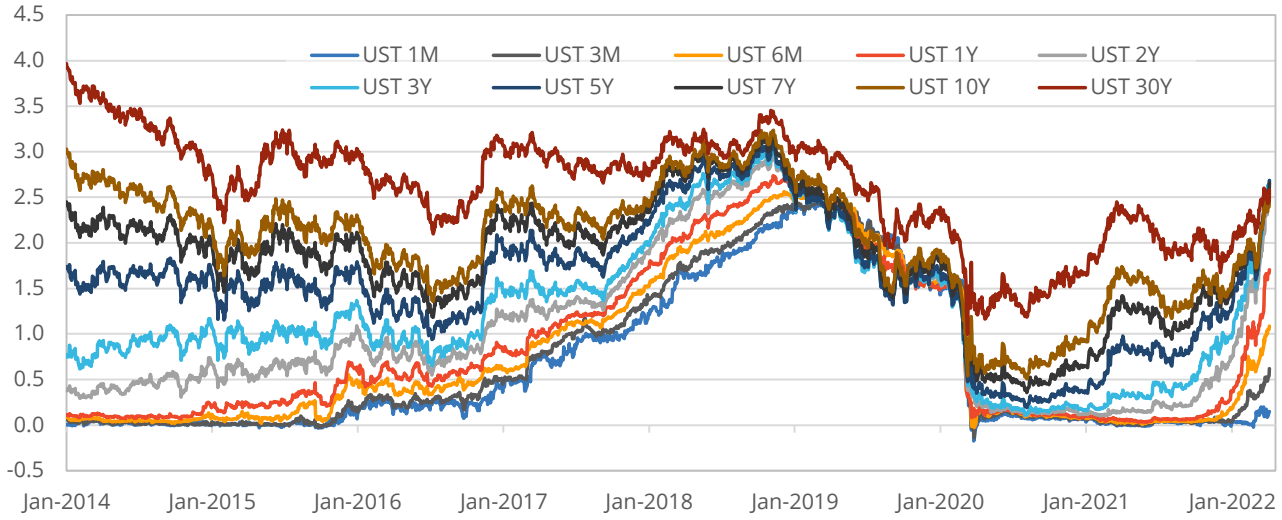
**Average 30Y Mortgage Rates**




*Source: Bloomberg, Bulltick*

The yield curve has flattened markedly, with the spread between 30s and 10s nearly non-existent at 2bps, and the 30-2s spread at just 5bps, after briefly turning negative last week. While an inverted yield curve has been one of the most consistent indicators of recession in years past, we only expect a sharp slowdown in growth in 2022, with forecasts further afield dependent on the Fed's success or failure at reining in inflation.

**US Yield Curve**



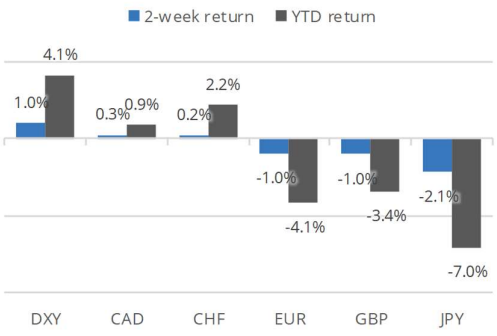
# FX Strategy:

- ***The ongoing determinant forces for the DXY remain:*** 1) The pace and magnitude of the Fed tightening cycle as well as balance sheet reduction and 2) Russia-Ukraine conflict. A quick resolution on the latter front is unlikely and that uncertainty will prevail over the medium term. Both factors are near-term supportive of the DXY (negative Euro). The Fed has already kicked off the tightening cycle, which we expect to accelerate to a 50bp pace of hikes, taking fed funds to 2.00% by year-end 2022.

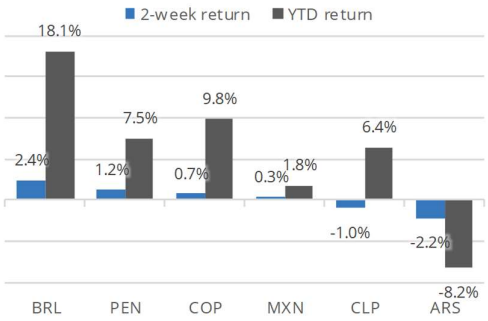
- ***We have updated our DXY forecast to 98 from 95 give the rising interest rate differential between the overnight rate in the US and the European intervention rate.*** The Fed's hiking cycle will run far ahead of that of the ECB. We expect multiple 50bp rate hikes in the US compared to a still on-hold European central bank. The latter will be reluctant to hike rates given the ongoing economic threat to the Eurozone of a potential closure of oil and gas imports from Russia. Europe, especially Germany, have made themselves highly vulnerable to energy exports from Russia and an even partial closure of the natural gas pipelines that run through Ukraine would have tremendous recessionary impulses for the Eurozone. Interest rate differentials with the US will grow, positive for the USD v. Euro.

- ***Meanwhile, EM currencies and some DM ones such as CAD and AUD*** will continue to be supported by high commodity prices. We con tinue to like COP and BRL, which despite recent run-up we view as still undervalued.

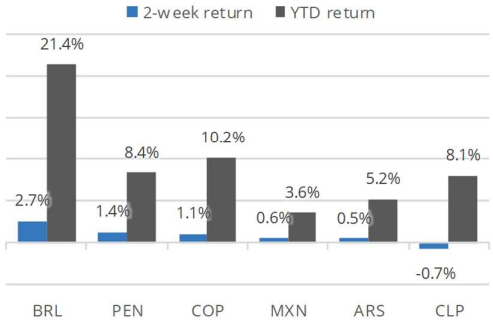
**Developed Markets, FX Spot Returns**




**Emerging Markets, FX Spot Returns**




**Emerging Markets, FX Carry Returns**

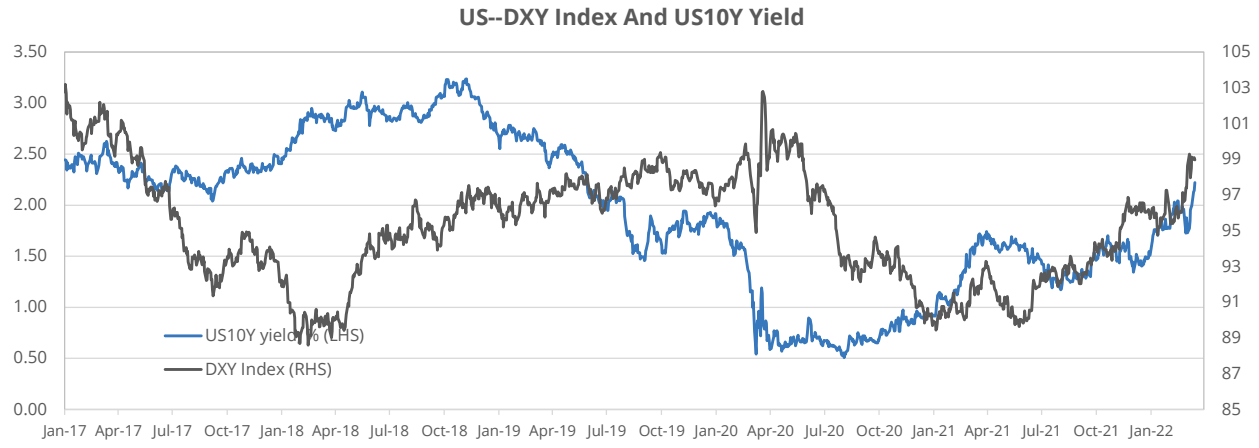



| Asset | Begin 2022 | Current | YTD Spot Return | YTD Interest Gains | End-2022 Target | 2022 Expected Spot Return | 2022 Expected Total Return |
|---|---|---|---|---|---|---|---|
| DXY | 95.7 | 99.6 | 4.1% | - | 98.0 | -0.7% | - |
| USD/EUR | 1.14 | 1.09 | -4.1% | -0.13% | 1.18 | 3.8% | 3.3% |
| JPY/USD | 115.1 | 123.8 | -7.0% | -0.02% | 115.0 | 0.1% | 0.0% |
| CNY/USD | 6.36 | 6.36 | -0.1% | - | 6.50 | -2.2% | - |
| MXN/USD | 20.52 | 20.15 | 1.8% | 1.88% | 22.00 | -6.7% | -0.4% |
| BRL/USD | 5.57 | 4.72 | 18.1% | 2.98% | 5.20 | 7.1% | 22.0% |
| COP/USD | 4,122 | 3,753 | 9.8% | 1.43% | 3700 | 11.4% | 17.8% |
| CLP/USD | 852.0 | 800.4 | 6.4% | 1.64% | 800.0 | 6.5% | 12.2% |
| PEN/USD | 4.00 | 3.72 | 7.5% | 0.91% | 3.90 | 2.6% | 7.6% |
| ARS/USD | 103.09 | 112.36 | -8.2% | 14.66% | 140.00 | -26.4% | 0.5% |

*Source: Bloomberg, Bulltick. Note: Total returns include 3m deposit (or comparable) interest gains. Carry gains incorporate interest rate differential with US rates. All FX returns are against USD*

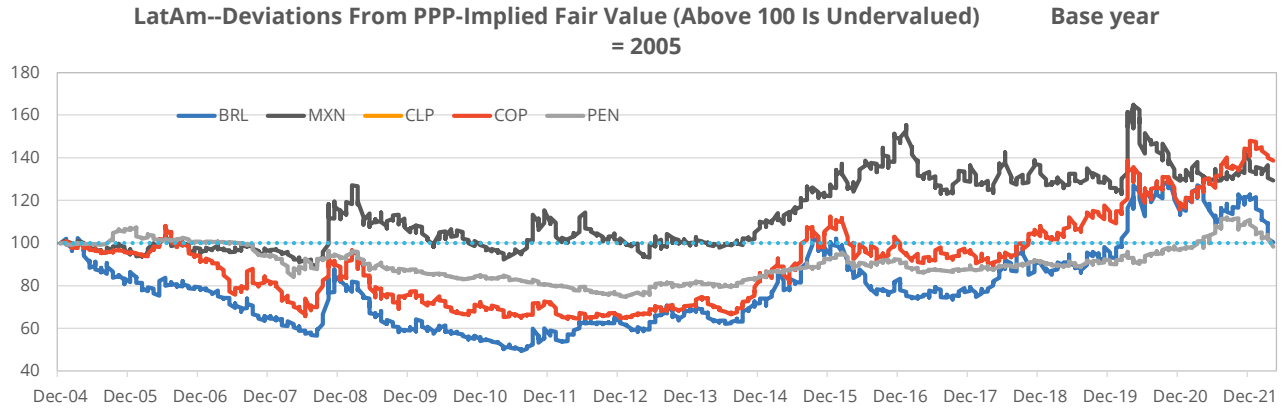
*As of 04/06/2022*

We expect the 10-year Treasury yield to continue to ascend through year-end 2022, rising to 2.75%. With it and given the rising interest rate differential between the US and Europe, upside pressure we expect to overcome countervailing depreciation forces to keep the DXY strong through December. Geopolitical risk could keep currencies volatile with the safe haven status pressuring JPY and USD in times of stress.




*Source: Bloomberg*

Within the emerging space, we see upside in commodity-exporters, particularly in Colombia and Brazil, where politics remain at the forefront of investors' minds but where we see potential for positive market surprises. Colombian elections favor left-wing Petro but recent polls show the possibility for a surprise while in Brazil, a re-election of former President Lula is not going to derail the economy.




*Source: Bloomberg, Bulltick*

# Equities Strategy:

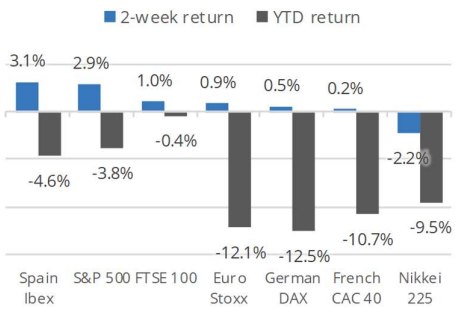
- ***We recommend more defensive positioning ahead of more aggressive, 50bps Fed hikes into an increasingly stagflationary environment.*** We recommend overweight positions in Energy, Staples, Utilities and Healthcare. Communication Services, Technology, Banks and Consumer Discretionary we expect to underperform in an environment of rising intervention rates and slowing economic growth. The cyclicals/value ratio is showing a rotation along these lines. (See the following page.) with a clear underperformance year-to-date for cyclicals versus more defensive sectors.

- ***Europe has seen a record outflow in portfolio capital*** given its exposure to the Russian conflict in Ukraine and higher energy costs. Europe will outperform when a resolution or accord is struck but that is as yet not clear in the near term. Value hunters may, however, start to look at Europe, betting on some eventual resolution and betting on an avoidance of full-scale cut-off of Russian energy exports. While negotiations are ongoing, there is no resolution in sight between Russia, NATO, and Ukraine, keeping volatility in oil prices and risk appetite high.

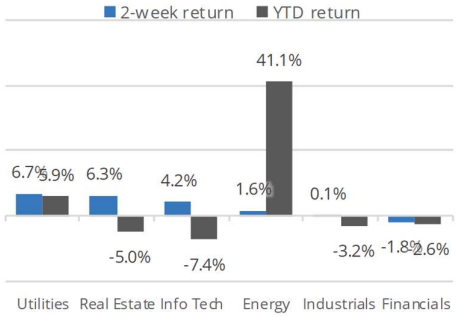
- In the Emerging space, while EM will remain under pressure, but we like certain names with exposure to the higher-commodity price theme, such as quasi-sovereign energy exporters in the region.

- ***The collapse in US consumer and business confidence numbers are concerning*** and bode poorly for a continuation of the post-Covid re-opening trends for discretionary. Inflation is a persistent and pernicious force that is digging into the ability for the consumer to spend on non-essentials.

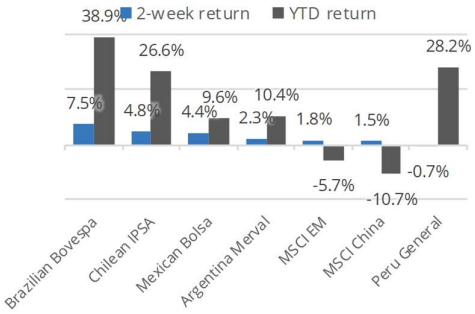
**Developed Market Equity Returns**




**Select S&P 500 Sectors Returns**




**Emerging Market Equity Returns**




| Asset | Div Yld | Begin 2022 Price | Current Price | Cap Gains (LCY, YTD) | Cap Gains (USD, YTD) | Target 2022 | 2022 Expected Total Returns LCY | w/Div | USD | w/Div |
|---|---|---|---|---|---|---|---|---|---|---|
| S&P 500 | 1.4% | 4,766 | 4,584 | -3.8% | -3.8% | 4,700 | -1.4% | -0.1% | -1.4% | -0.1% |
| Euro Stoxx | 3.3% | 4,298 | 3,915 | -8.9% | -12.1% | 5,000 | 16.3% | 19.1% | 20.7% | 23.6% |
| German DAX | 3.2% | 15,885 | 14,406 | -9.3% | -12.5% | 18,000 | 13.3% | 16.0% | 17.6% | 20.4% |
| Nikkei 225 | 2.1% | 28,792 | 27,788 | -3.5% | -9.5% | 32,000 | 11.1% | 13.0% | 11.3% | 13.1% |
| Shanghai Comp | 3.1% | 3,640 | 3,283 | -9.8% | -9.9% | 4,100 | 12.6% | 15.0% | 10.1% | 12.4% |
| MSCI India | 1.4% | 2,037 | 2,088 | 2.5% | 1.5% | 2,250 | 10.5% | 11.7% | 7.3% | 8.5% |
| MSCI EM | 2.9% | 1,232 | 1,162 | -5.7% | -5.7% | 1,450 | 17.7% | 20.5% | 17.7% | 20.5% |
| MSCI World | 2.0% | 755 | 719 | -4.8% | -4.8% | 836 | 10.7% | 12.6% | 10.7% | 12.6% |
| Mexican Bolsa | 3.3% | 53,272 | 56,313 | 5.7% | 9.6% | 56,000 | 5.1% | 7.9% | -2.0% | 0.6% |
| Brazilian Bovespa | 6.7% | 104,822 | 121,125 | 15.6% | 38.9% | 120,000 | 14.5% | 22.1% | 22.6% | 30.8% |
| Colombia COLCAP | 5.2% | 1,411 | 1,621 | 14.9% | 27.7% | 1,400 | -0.8% | 2.6% | 4.9% | 8.5% |

*Source: Bloomberg, Bulltick. Chart returns are in USD, excluding dividends* *As of 04/06/2022*

We have updated our S&P 500 sector views and have overweights on those sectors that historically outperform in stagflationary scenarios: utilities, staples, healthcare, and energy. We have moved marketweight on tech and UW in communication services and discretionary given these sectors' less favorable historical returns in a slowing economy with high inflatin and rising fed funds rates. We recommend marketweight positions in industrials, real estate (which has countervailing forces at play, leaning to the downside), and financials (which was our top pick and top performing sector in 2021.)

## S&P 500 Sector Valuations

| S&P Benchmark Indices | SPX Weight | Current Fwd PE Ratio | Average (60M) Fwd PE Ratio | Percent of Average | Weighted EPS Trajectory | Bulltick 2022 View |
|---|---|---|---|---|---|---|
| S&P 500 Index | 100.00 | 20.28 | 19.94 | 101.7% | ↑ | |
| S&P 500 Info Tech Index | 28.03 | 25.94 | 22.72 | 114.2% | ↑ | MW |
| S&P 500 Health Care Idx | 13.51 | 16.56 | 16.67 | 99.4% | ↑ | OW |
| S&P 500 Cons Discret Idx | 12.14 | 28.54 | 28.22 | 101.1% | ↑ | UW |
| S&P 500 Financials Index | 10.89 | 14.60 | 14.01 | 104.2% | ↑ | MW |
| S&P 500 Comm Svc | 9.52 | 18.58 | 17.53 | 106.0% | ↑ | UW |
| S&P 500 Industrials Idx | 7.73 | 20.85 | 22.38 | 93.1% | ↑ | MW |
| S&P 500 Cons Staples Idx | 6.09 | 22.25 | 20.21 | 110.1% | ↑ | OW |
| S&P 500 Energy Index | 3.92 | 10.97 | 25.87 | 42.4% | ↑ | OW |
| S&P 500 Real Estate Idx | 2.79 | 46.43 | 42.55 | 109.1% | ↑ | MW |
| S&P 500 Utilities Index | 2.76 | 22.17 | 18.78 | 118.1% | ↑ | OW |
| S&P 500 Materials Index | 2.63 | 15.90 | 18.85 | 84.3% | ↑ | OW |

The cyclicals/defensives sectors ratio is showing an outperformance of value with a year-to-date return of -1.6%. Indeed, we recommend overweight positions in defensive sectors including Energy, Staples, Utilities and Healthcare. Communication Services, Technology, Banks and Consumer Discretionary we expect to underperform in an environment of rising intervention rates and slowing economic growth.

**SPX Cyclical/Defensive Stocks Ratio (YTD Gains=-1.61%)**


*Source: Bloomberg, Bulltick*

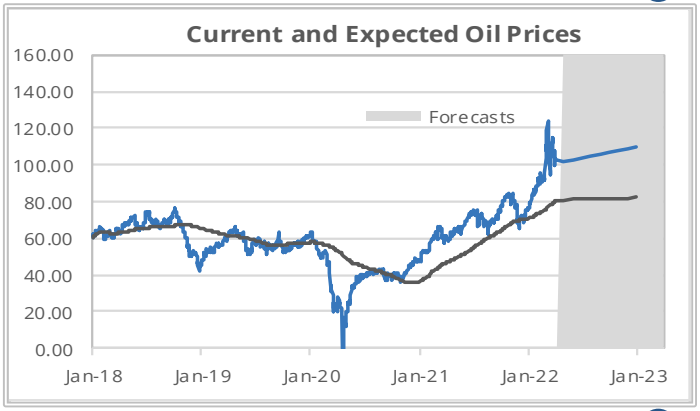
# Alternative Investments

① ***Extreme volatility has characterized oil over the past several weeks,*** most notably due to the prospect of supply disruptions in Europe amid the ongoing conflict in Ukraine. Europe is highly dependent on Russian oil, and despite escalating sanctions against his country to punish Russian President Vladimir Putin's aggression, the energy sector has been spared. This may change, particularly if recent stories of serious war crimes are verified and repeated. As such, we believe that the risks to oil prices are weighted to the upside, with a 'fat tail' risk of a return to US$120+ prices for WTI. Our core scenario, and our forecast, is for WTI to end the year at US$110/bbl.

② ***Rig counts in the US are coming back online, but will struggle to keep pace with demand,*** particularly if further supplies are needed to keep the lights on in Europe. US production growth has also been slow due to environmental priorities by the Biden administration. We expect the political calculus to change amid soaring pump prices, and for restrictions to ease, but this will take time to have an impact on global prices.

③ ***Precious metals have come off their recent highs, as UST yields have climbed,*** reducing the appeal of non-yielding safe-havens. Nevertheless, we expect that inflation is here to stay for the next several years, and that gold should be part of an inflation-hedge strategy, along with real assets and even cryptocurrency.

#1

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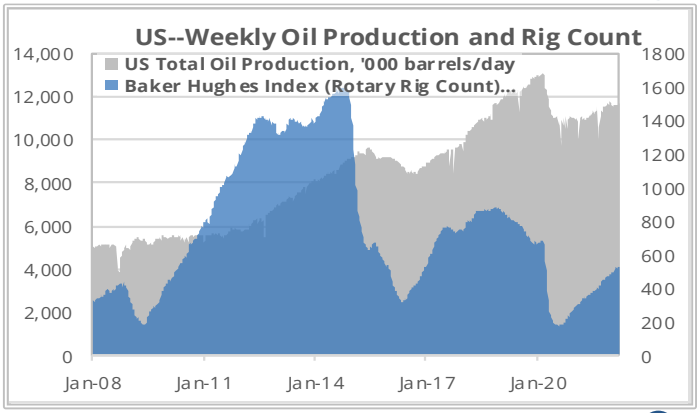


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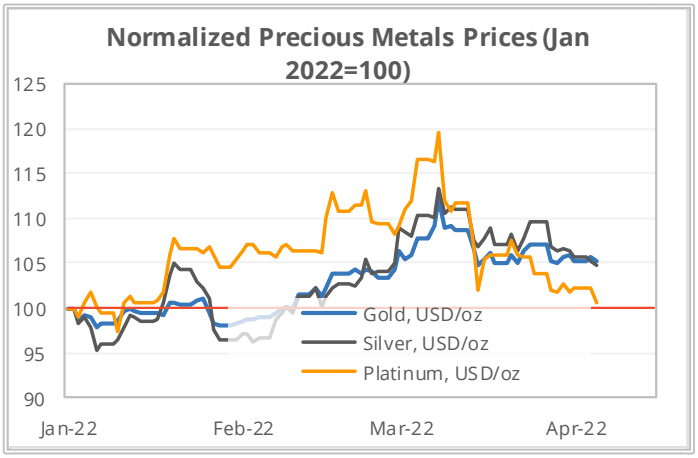


*Source: Bloomberg, Bulltick*

*As of 04/05/2022*

# About us & contacts

## About Bulltick Capital Markets

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## Our Research Resources

With Bulltick's vast Latin American in-roads, resources and networks, our research team is strategically positioned to provide value-added research on local and regional companies, markets and industries. With analysts in the region, along with management road shows, we are able to track the pulse of the leading markets in Latin America. We make it our business to know the business of the region, so we can help our clients manage volatility with in-depth coverage of macroeconomic leading sectors and market-moving events.

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