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Bulltick Research and Strategy

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Global Cross Asset Strategy:

Recession Inevitable But Not Imminent

Of the recessionary indicators we follow closely, the majority do not yet point to imminent or near-term recession. Economic contraction is part of the economic cycle, and we maintain our conviction view that we are in decelerating part of the cycle, having reached (and passed) the peak. However, we believe recession is not a 2022 event and much depends on the Fed.

Consumer confidence measures are showing warning signs on the future of the US consumer. Inflation is forcing more dollars to exit purses and the savings rate to decline, which we saw demonstrated in last week's US savings rate data.

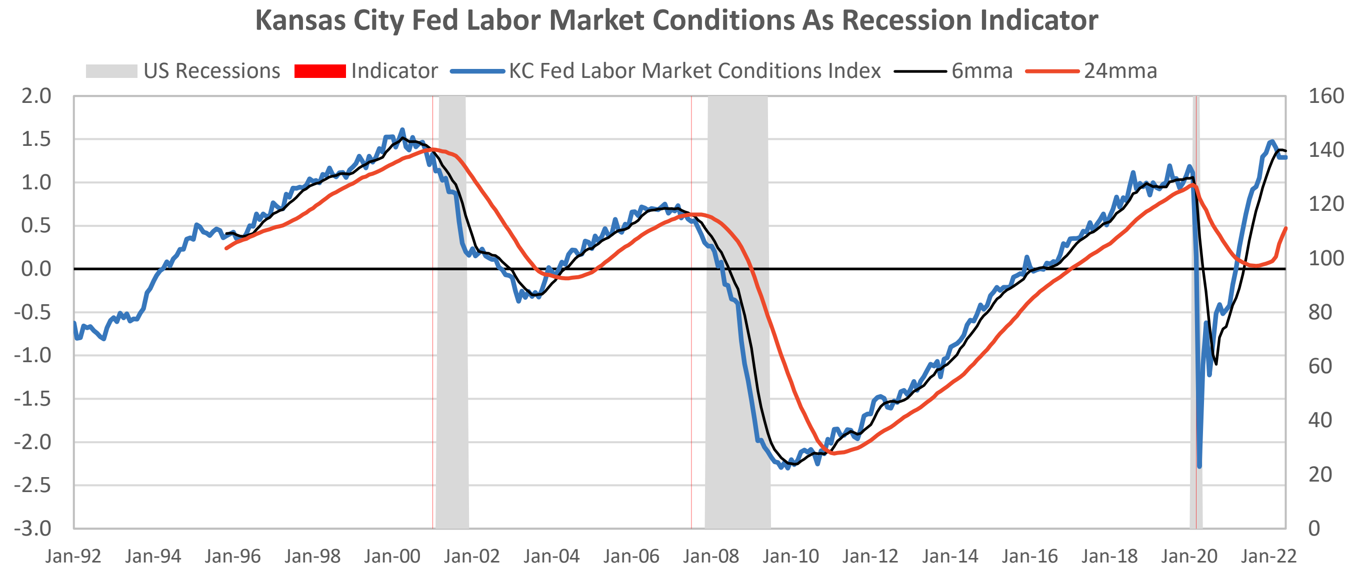
What could speed up or slow down the Fed's two-pronged policy tightening? Read on for our analysis. Listen to our markets outlook and recession analysis here.

Asset	Spot	Chg In Past 2 Weeks	YTD Change	End- 2022 Target
USG10Y	2.93	+5bps	+142bps	2.75
USG30Y	3.09	+2bps	+118bps	3.25
JGB10Y	0.24	-1bps	+17bps	0.10
DXY	102.50	-1.26%	7.14%	98.00
EUR	1.07	1.83%	-6.28%	1.18
JPY	130.15	-1.47%	-11.57%	115.00
MXN	19.69	1.79%	4.29%	20.50
BRL	4.80	3.50%	16.00%	5.20
SPX	4124	5.11%	-13.47%	4700
IBOV	111689	5.12%	6.55%	120000
MEXBOL	51475	2.15%	-3.37%	56000
Brazil 10Y	12.69	+24bps	+190bps	11.75
Mexico 10Y	8.68	-17bps	+112bps	8.50
MXEF	1078	4.31%	-12.53%	1450
Gold	1848	1.71%	1.00%	1950
WTI Crude	115.1	5.06%	53.09%	110.0

As of 06/01/2022

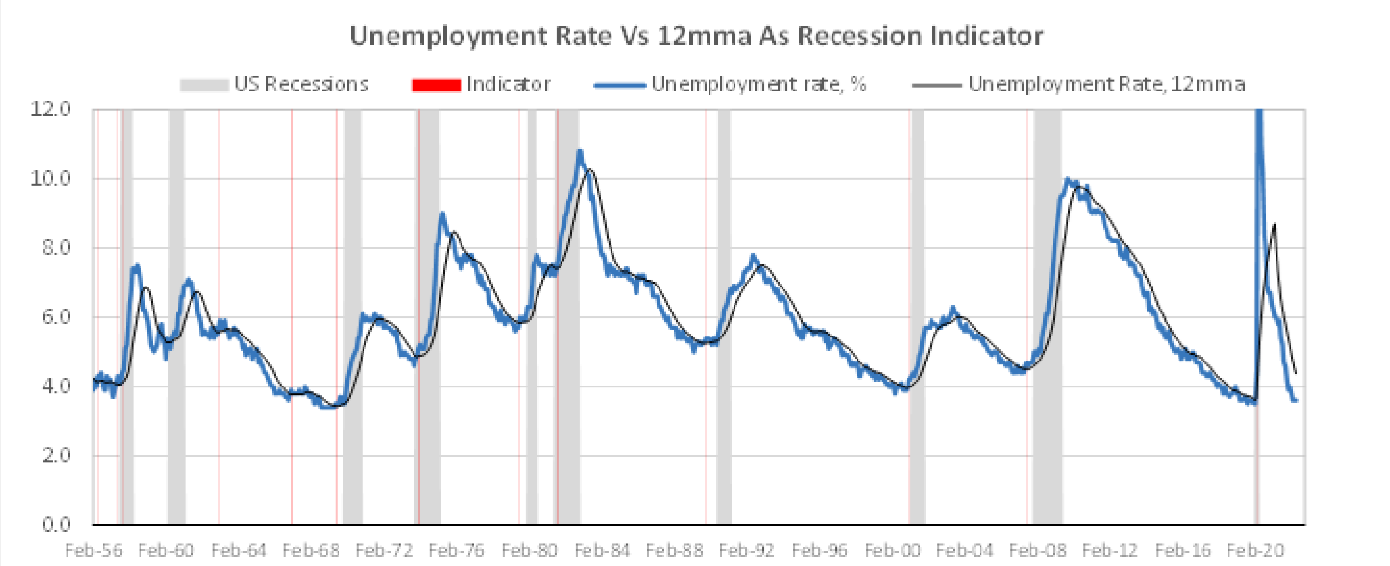
bulltick

Recession indicators. The labor market is remains non-threatening, with the 6month/24month cross of the labor market conditions index still far from triggering:



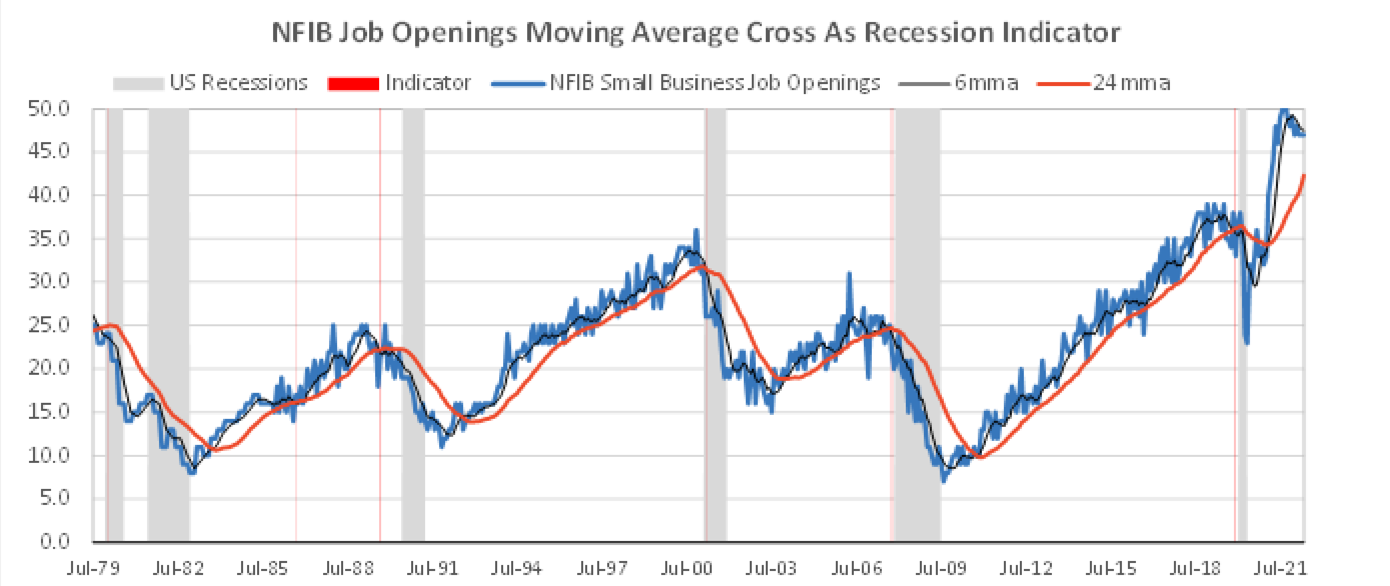
Source: Bloomberg, Bulltick

The unemployment rate indicator trigger is when unemployment crosses the 12mma:



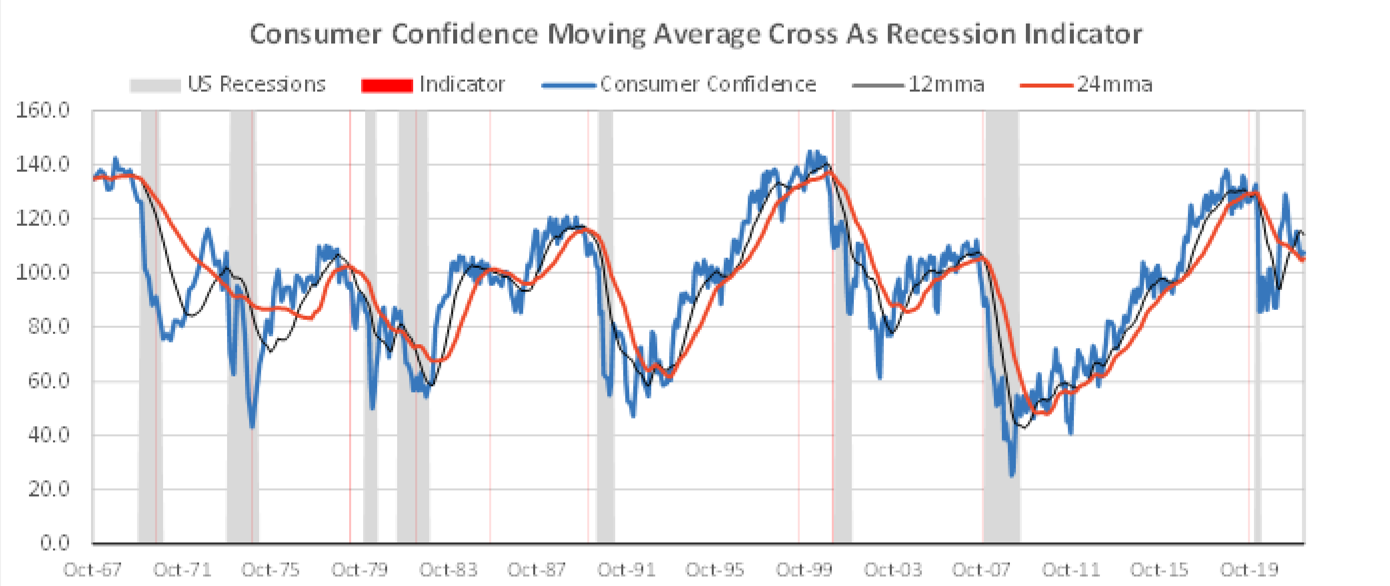
Source: Bloomberg, Bulltick

NFIB jobs 6m/24m cross does not point to imminent recession:

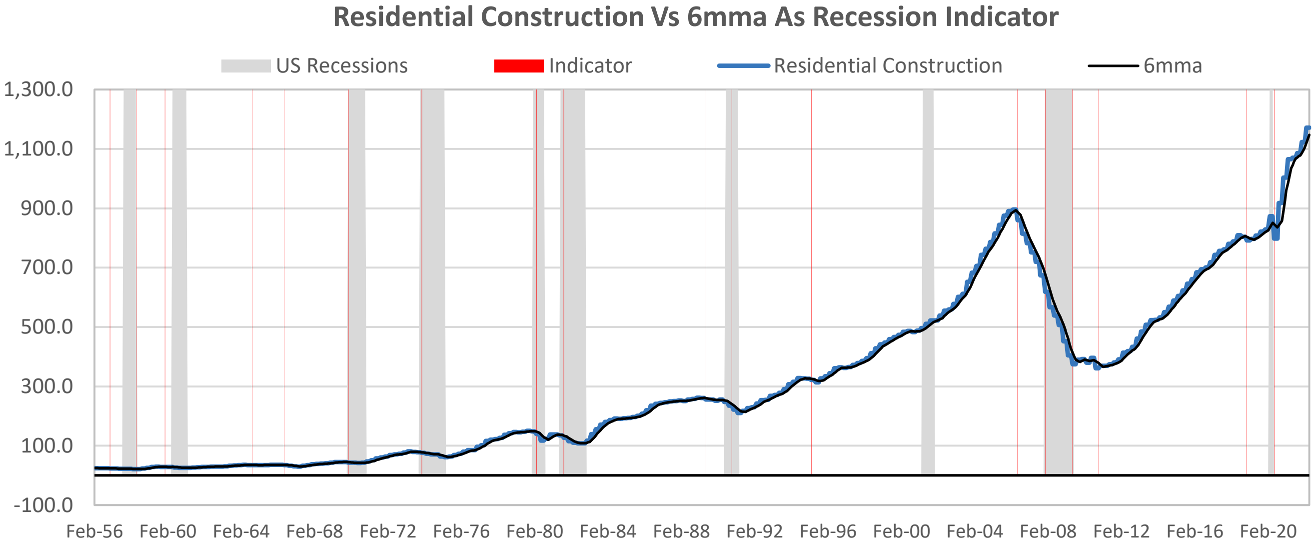


Source: Bloomberg, Bulltick

Of course, all of these labor market indicators are a function of the pandemic, which saw very extreme, very short-lived disruptions to trends, which are still being phased out in the moving averages. But others are also encouraging, such as the Consumer Confidence crosses, and housing:

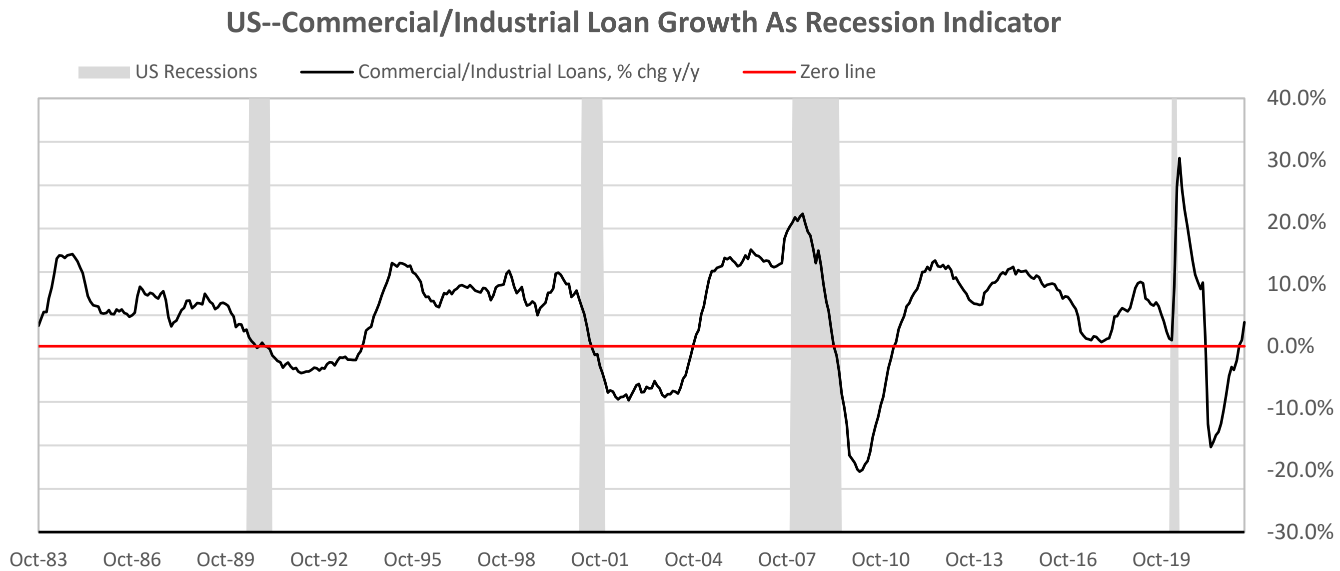


Source: Bloomberg, Bulltick

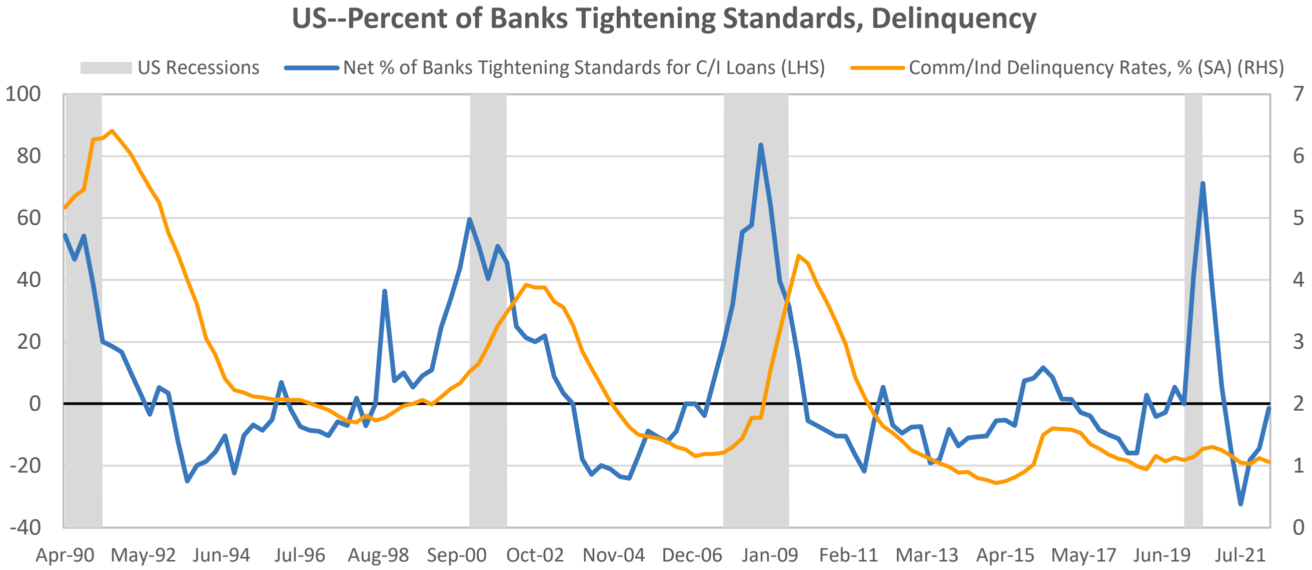


Source: Bloomberg, Bulltick

Loan growth is one of the indicators more directly impacted by Fed hikes. Historically, recessions are associated with steep declines in loan growth and a tightening of lending standards. That loan growth fell so much before the hiking cycle began seems to indicate that the Fed is going to have a hard time impacting it, apart from causing loan recovery to be slower. Another indicator that the transmission mechanism is shaky this cycle. Firms have plenty of cash on hand and are less likely to need financing.



Source: Bloomberg, CBO, Bulltick



Source: Bloomberg, Federal Reserve, Bulltick

***Fed Analysis* -** If the Fed hikes rates and rolls off bonds too aggressively, near term risks of recession rise. So far the Fed has appeared ready and willing to hike rates including at a 50bp clip, even considering 75bps. But what could cause the Fed to pull up the reins from its double whammy of QT and rate hikes this year, i.e. What could make the Fed more dovish?

Double barreled tightening refers to rate hikes and balance sheet unwind. Futures indicate markets expect fed funds at 3.00% by early next year. Meanwhile, starting this month, the Fed is set to let bonds roll off to $95 billion/month. That is a lot. On both fronts.

The Fed got behind on inflation. Now they either hike and tighten (QT), risking a recession or stand down and let inflation do what it's going to do anyway. BullTick research estimates inflation to end the year at 4.7% (core PCR). We contend that the Fed has limited control over the Cpi basket anyway (and not just census of oil, food, and supply change disruptions!). That means if they suddenly and belatedly become inflation fighters now they run a real risk of throwing the economy into recession sooner.

What could cause the fed to slow up on the double-barreled monetary policy tightening? Our thoughts: 1) bear market, big correction, credit gaps out as tightening financial conditions blow out spreads and equities markets 2) a rollover in the job market. Unemployment jump is a leading indicator of recession. Fed likely pause is simultaneous rate hikes and QT. 3) Rates have already risen from USTs to mortgages to consumer loans, and with only 75bps in rate hikes (from 0%.) These higher rates and tightening financial conditions could (should) slow economic growth so the Fed doesn't have to take rates up as much as consensus expects (more or less 250bps for entire 2022).

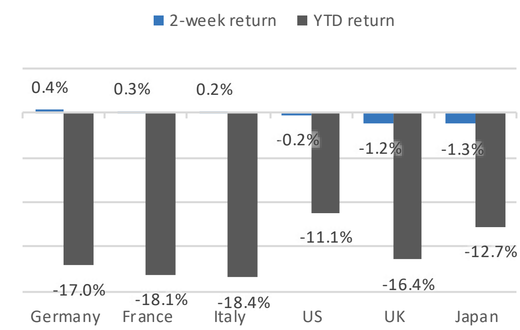
Fixed Income Strategy:

- ***In the past month, US Treasury yields have again seen significant movement, trading within a 40-50bps range.*** Early last month the 10 year note broke the top of the range, trading above 3% after the Fed's comments and on the back of strong employment data. The 3.19% print on May 9th was the highest yield on the 10 year note since 2018. This yield ascent made an already-beaten up fixed income asset class suffer more.

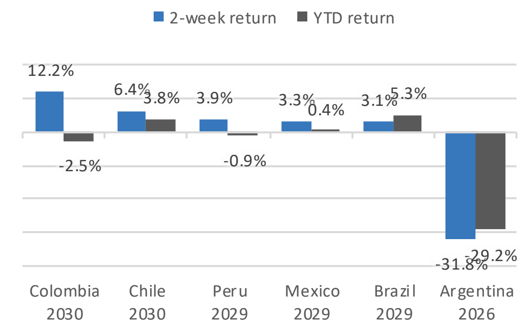
- **From nearly 3.20% in early May to 2.73% towards the end of the month**, both technical factors and poor economic data were the main drivers of UST yield movements. "Recession" is the new zeitgeist in market chatter. Our trading desk reports that moves of this magnitude (40-50bps) normally would incite some significant buying into the bond market, but given the speed of the move and uncertainty in the markets, flows have been moderate.

- ***In a decelerating economy combined with rate hikes and a Fed in "quantitative tightening" mode***, fixed income is an asset class that will continue to suffer. We expect that higher financing costs combined with an increasingly difficult environment to generate profits will lead to some debt defaults. For this reason, our House view is that today more than ever it is critical to be positioned in names that have good fundamentals and that can withstand rising rates and low demand.

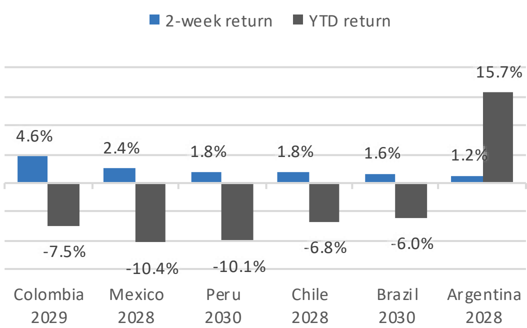
Developed Markets 10Y Total Returns



EM Local Currency Bond Total Returns



EM USD-Denominated Bond Total Returns

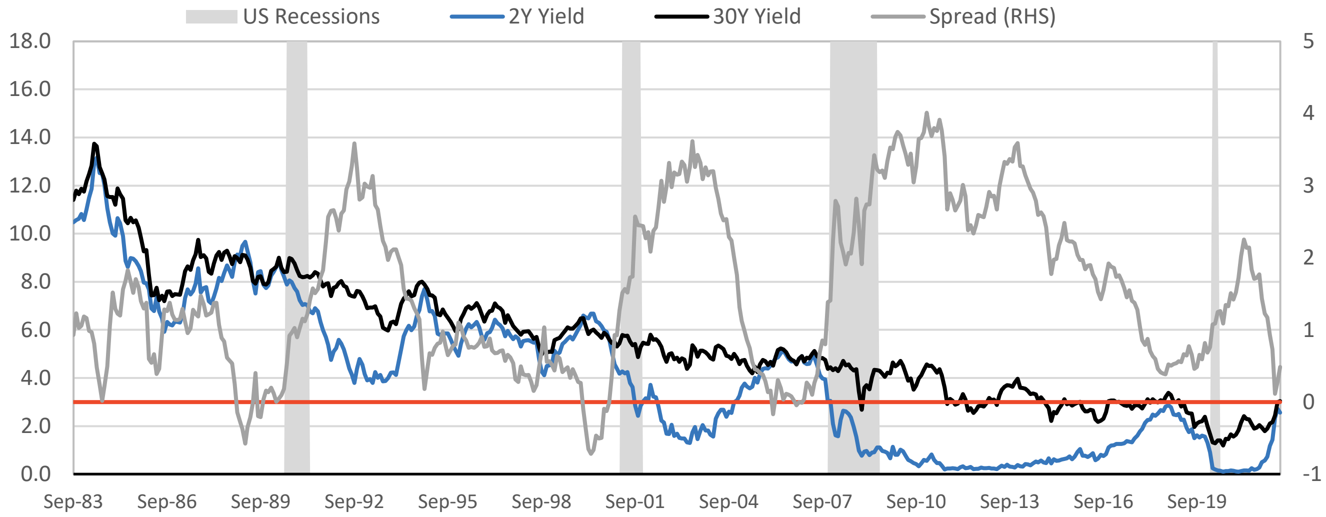


Benchmark Asset	Begin-2022 YTM	Current YTM	YTD Interest Gains, %	YTD Capital Gains, %	YTD Forex Gains, %	Total YTD Return, %	2022 Target YTM	2022 Return, %
UST 10Y	1.51	2.94	0.59%	-11.71%	-	-11.12%	3.00	-11.33%
German 10Y	-0.18	1.14	0.00%	-11.48%	-6.29%	-17.05%	-0.20	4.02%
Japan 10Y	0.07	0.22	0.04%	-1.42%	-11.52%	-12.74%	0.10	-0.14%
Mexico MBONO 2031	7.56	8.68	3.23%	-6.96%	4.27%	0.38%	8.50	1.72%
Mexico USD, 2031	2.95	4.53	1.15%	-11.59%	-	-10.44%	3.10	1.48%
Brazil BRL 2031	10.84	12.69	4.41%	-4.91%	16.27%	15.70%	11.75	17.14%
Colombia TES 2031	6.34	10.64	2.96%	-23.66%	8.43%	-14.01%	8.00	1.37%
Chile CLP 2032	5.65	6.28	2.45%	-2.01%	3.39%	3.85%	6.00	9.33%
Argentina ARS, 2026	49.55	57.43	15.35%	-13.67%	-14.43%	-13.00%	50.00	-6.05%
Peru Soberano 2031	5.90	7.53	2.73%	-10.44%	7.35%	-0.94%	6.00	8.54%

Source: Bloomberg, Bulltick. All returns are in USD *As of 06/01/2022*

We expect Treasury rates to be range bound (2.70% to 3%) in the near-term months due to a decelerating economy; it is very likely that the FED will have to be less aggressive in its double-barreled policy response to high and sticky inflation. In the fixed income space, our House view favors a more defensive tilt to a portfolio in terms of both sectors and in terms of debt serviceability. We are keeping a close eye on thee yield curve, which has come up from inversion on the 2s/30s space back into positive territory.

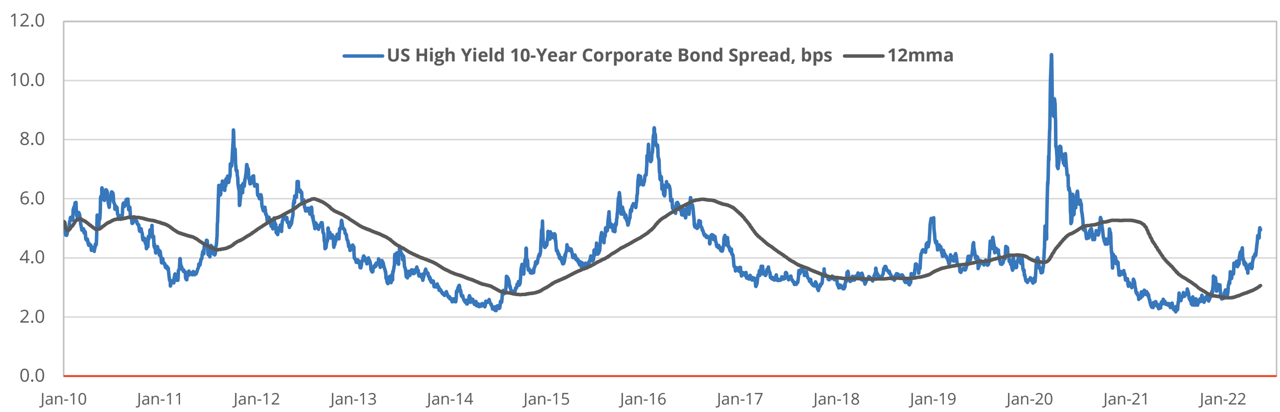
30 and 2 Year Bond Yield Spread



Source: Bloomberg, Bulltick

Credit spread blowouts and the potential for a more signficant drop in equity markets could put the Fed on hold in terms of its rate hike and asset rolloff. Credit risk concerns have yet to peak, as illustrated by HY corporate bond spreads over USTs, which have continued to climb. As growth concerns increasingly accompany inflation concerns in the minds of investors, we expect such trends to persist.

US HY Corp 10Y Bond Spread Over UST



Source: Bloomberg, Bulltick

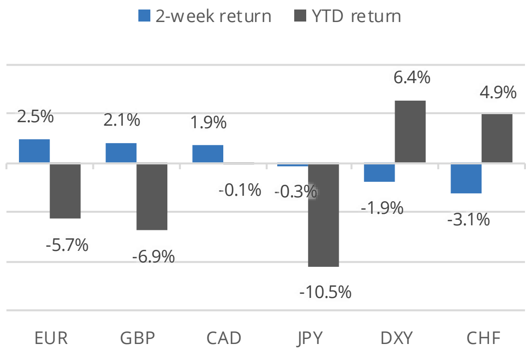
FX Strategy:

- ***Poor inflation prints and bets on a hawkish Fed*** have moved DXY higher against all majors and EM FX in recent trading. The hand of the Fed has indeed been forced as we in Bulltick Research have been forecasting for some time because the Fed got behind inflation and miscalculated its drivers. Now the question is how far will the Fed hike and much will it allow to roll off its balance sheet before inducing recession in the US economy. The USD strength of late is due to the high interest rate differential it enjoys over peers in Europe and Japan. USD will remain strong this year as that differential continues to be wide.

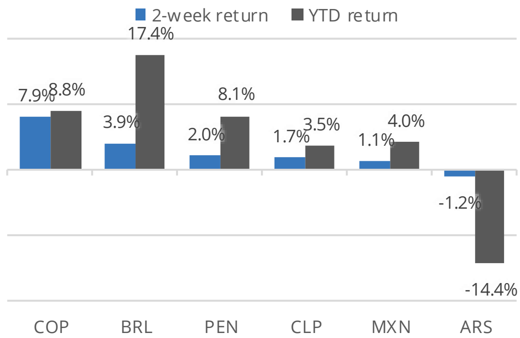
- ***JPY has been particularly hard hit, trading at a two-week low*** v. USD, breaking 130 and falling the most in the G10 currencies in the past two weeks. It is all about interest rate differential with divergent central banks; the Fed is hawkish and the BOJ remains ultra-dovish. We expect these trends to continue for the rest of the year.

- ***Hit by risk-off sentiment, LatAm FX has seen an off two weeks with heavyweight Brazil leading recent losses*** (despite remaining the best performing currency YTD the region) as the market prices in a smaller carry for EM FX as the Fed hikes rates. Its commodity status and the massive interest rate differential versus the USD favor the Real and we see the SELIC of 12.75%, and likely to move yet higher to 13.25%. Brazil faces presidential election in October but either outcome we think is market neutral. WE believe Lula will win and this is already baked into prices. Stay positive BRL.

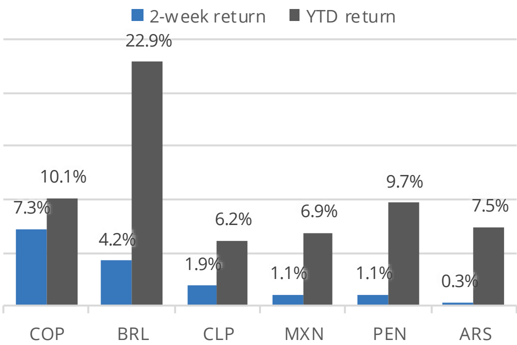
Developed Markets, FX Spot Returns



Emerging Markets, FX Spot Returns



Emerging Markets, FX Carry Returns



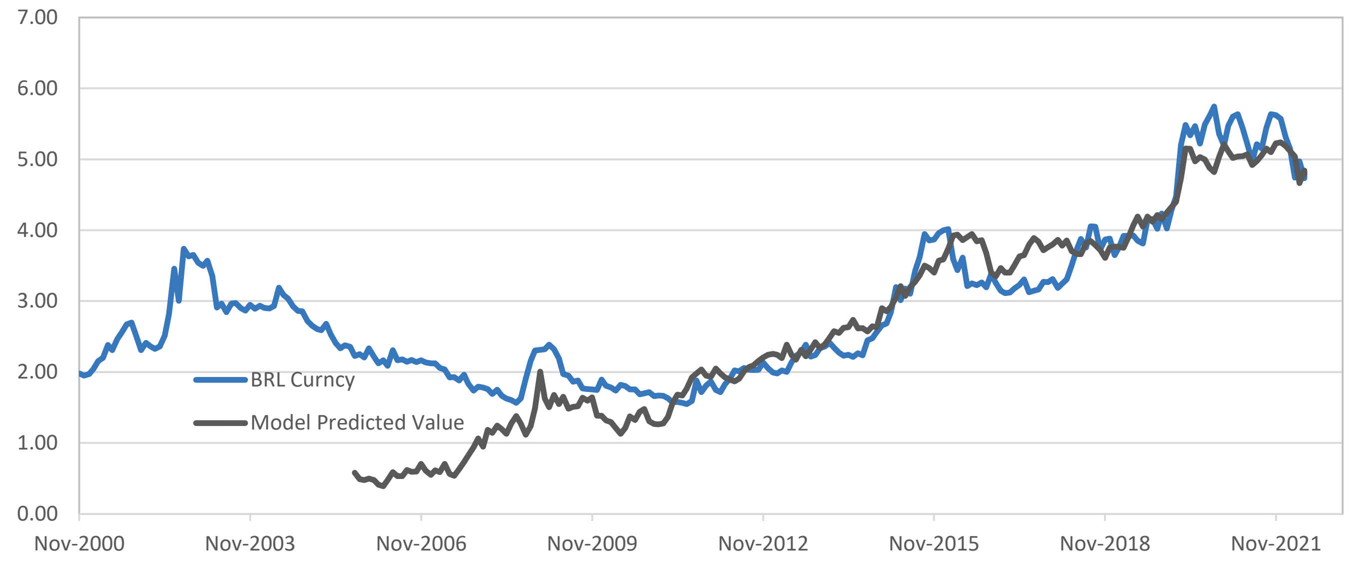
Asset	Begin 2022	Current	YTD Spot Return	YTD Interest Gains	End-2022 Target	2022 Expected Spot Return	2022 Expected Total Return
DXY	95.7	101.8	6.4%	-	95.0	-0.7%	-
USD/EUR	1.14	1.07	-5.7%	-0.20%	1.18	3.8%	3.3%
JPY/USD	115.1	128.6	-10.5%	-0.03%	115.0	0.1%	0.0%
CNY/USD	6.36	6.67	-4.7%	-	6.50	-2.2%	-
MXN/USD	20.52	19.72	4.0%	3.14%	20.50	0.1%	7.9%
BRL/USD	5.57	4.75	17.4%	4.94%	5.20	7.1%	23.6%
COP/USD	4,122	3,787	8.8%	2.51%	3900	5.7%	13.7%
CLP/USD	852.0	823.6	3.5%	2.91%	800.0	6.5%	14.2%
PEN/USD	4.00	3.70	8.1%	1.73%	3.90	2.6%	8.8%
ARS/USD	103.09	120.48	-14.4%	26.07%	140.00	-26.4%	10.3%

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 06/01/2022

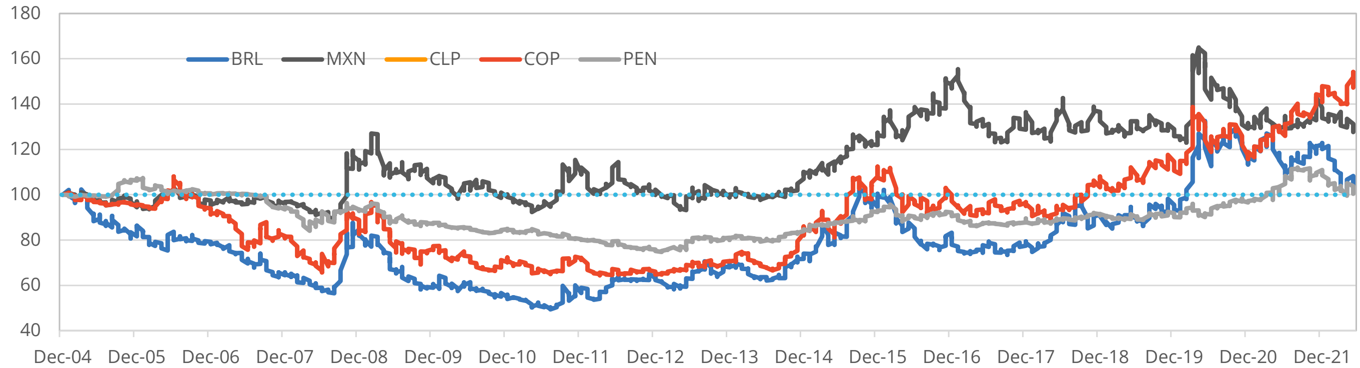
LatAm FX regional roundup: Regional currencies have been hit hard in recent weeks as the markets price in higher Fed funds rates and a weakening US economy with recession increasingly mentioned. The Real has been the worst performer in recent weeks (albeit still the best year-to-date). Our fair value models show the BRL currently very close to trading at fair value levels, which we calculate at 4.73/USD. The remarkably stable Mexican peso has slid as consensus inflation forecast has risen to 6.81% y/y for end-2022 (consensus sees economic growth at a mere +1.80%) – data as per a recent Banxico survey.

BRL-Actual Versus Predicted Values



The Peruvian sol and Chilean peso, both heavy copper commodity stories, followed suit, depreciating versus the USD despite lofty commodity price and demand and as both countries' economic growth data have surprised to the downside. The global growth slowdown after last year's re-opening boom combined with outlook for the carry these currencies have enjoyed are putting downside pressure on EM currencies despite a pickup in portfolio flows.

LatAm--Deviations From PPP-Implied Fair Value (Above 100 Is Undervalued) Base year = 2005



Source: Bloomberg, Bulltick

Equities Strategy:

- ***Valuation metrics, including the PE Ratio, for the S&P 500 are near long-term historical averages,*** stretching back into eras in which the index had a substantially lower weighting of tech stocks (which intuitively should have higher PE ratios given their dependence on future growth and innovation). Meanwhile, the index is up more than 5% from recent lows below 4,000 touched last week, as the market is debating whether we have seen the bottom.

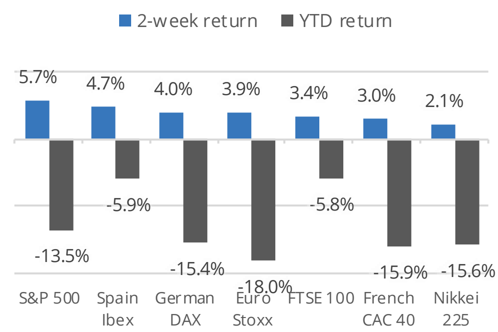
- ***With the Fed's QT just beginning, and inflationary pressures still substantial, we believe risks remain*** over the near term for another leg lower before re-risking returns in full force. We expect the PE Ratio, which currently stands at 18.0, may yet fall below the 17.0 mark amid increasing uncertainty.

- ***Nevertheless, investors would do well to begin to gradually reduce cash positions*** as we believe that further declines will be more modest than those we have seen in recent weeks, although we continue to favor defensive sectors, including healthcare, utilities, and consumer staples.

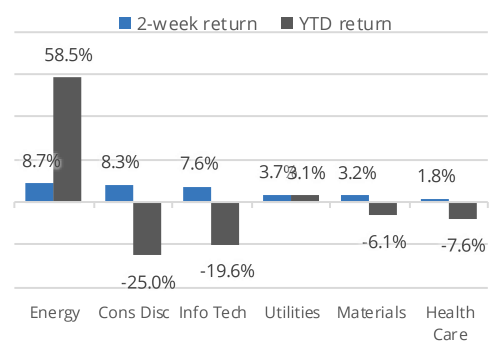
- ***All eyes will continue to be on the Fed,*** which will be a major driver of investor sentiment. We expect that continued aggressive rate hikes will persist, but that this has largely been priced into the market. Of more interest is if the nature of QT changes substantially in either pace or composition.

- ***Our top picks in LatAm are surging,*** thanks in large part to commodity tailwinds, although Colombia's recent bounce is more to do with political developments, as the (still likely-to-win) leftist Gustavo Petro was dealt a setback as populist Rodolfo Hernandez outperformed expectations in the first

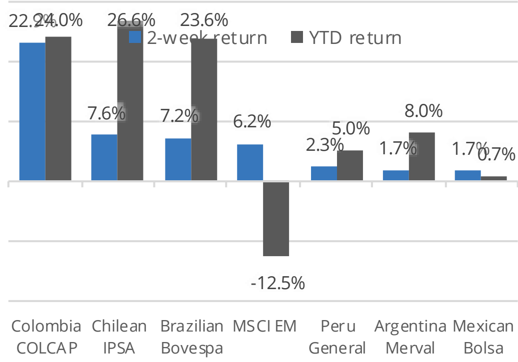
Developed Market Equity Returns



Select S&P 500 Sectors Returns



Emerging Market Equity Returns

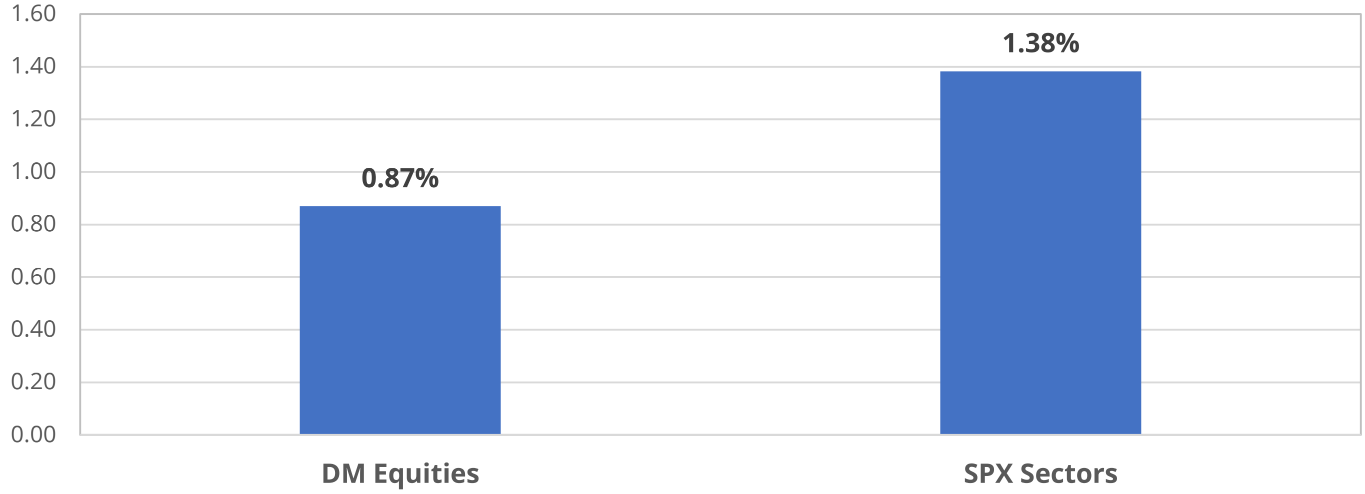


Asset	Div Yld	Begin 2022 Price	Current Price	Cap Gains (LCY, YTD)	Cap Gains (USD, YTD)	Target 2022	2022 Expected LCY	w/Div	Total Returns USD	w/Div
S&P 500	1.6%	4,766	4,124	-13.5%	-13.5%	4,700	-1.4%	-0.1%	-1.4%	-0.1%
Euro Stoxx	3.5%	4,298	3,760	-12.5%	-18.0%	4,200	-2.3%	0.5%	1.4%	4.3%
German DAX	3.4%	15,885	14,340	-9.7%	-15.4%	15,500	-2.4%	0.2%	1.3%	4.0%
Nikkei 225	2.2%	28,792	27,458	-4.6%	-15.6%	29,500	2.5%	4.3%	2.6%	4.4%
Shanghai Comp	2.9%	3,640	3,182	-12.6%	-16.9%	4,100	12.6%	15.0%	10.1%	12.4%
MSCI India	1.6%	2,037	1,925	-5.5%	-9.2%	2,250	10.5%	11.7%	6.6%	7.7%
MSCI EM	3.1%	1,232	1,078	-12.5%	-12.5%	1,450	17.7%	20.5%	17.7%	20.5%
MSCI World	2.2%	755	653	-13.5%	-13.5%	775	2.7%	4.5%	2.7%	4.5%
Mexican Bolsa	3.7%	53,272	51,475	-3.4%	0.7%	56,000	5.1%	7.9%	5.2%	8.0%
Brazilian Bovespa	8.2%	104,822	111,689	6.6%	23.6%	120,000	14.5%	22.1%	22.6%	30.8%
Colombia COLCAP	5.8%	1,411	1,613	14.3%	24.0%	1,400	-0.8%	2.6%	4.9%	8.5%

Source: Bloomberg, Bulltick. Chart returns are in USD, excluding dividends *As of 06/01/2022*

Over the past ten years, the intra-index, sector dispersion of monthly returns has been nearly 60% higher than the dispersion seen across the principal DM equity markets in the US, Europe, the UK, and Japan. As a result, beating the market is much more a factor of getting sector calls right than of investing with geographic preferences.

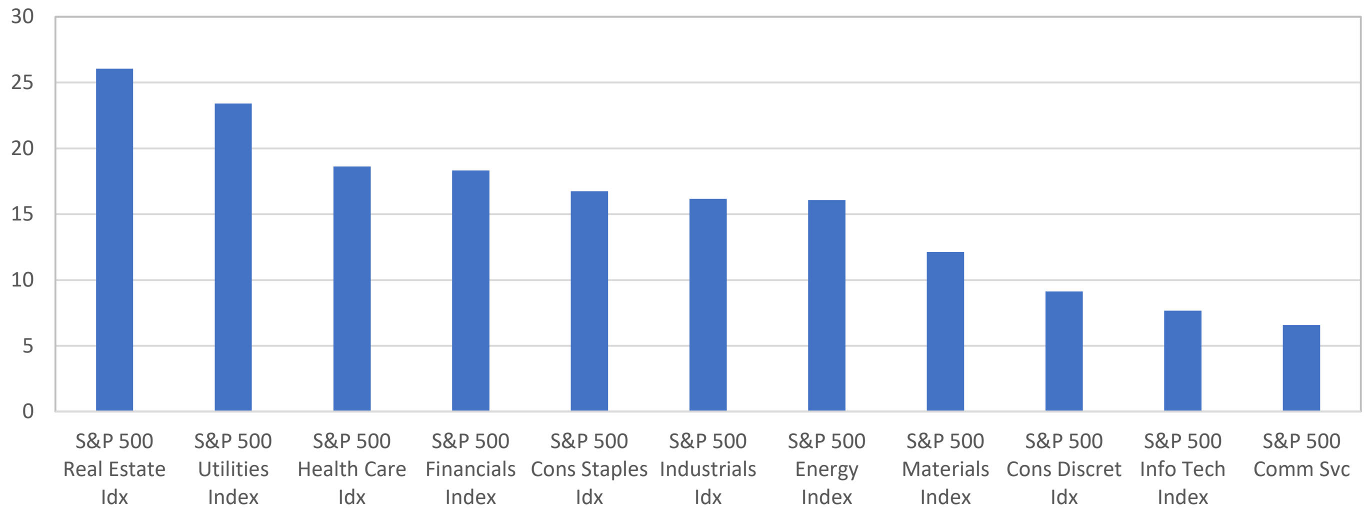
Average Cross-Asset Standard Deviation of Monthly Returns Over Past 10 Years, %



We expect the growth rates of forward-EPS estimates to continue to fall, and substantially. In past instances where this has been the case, Utilities and Health Care, two of our preferred sectors presently, have tended to outperform the broad index.

Average Sector Returns, 12m following past EPS peaks

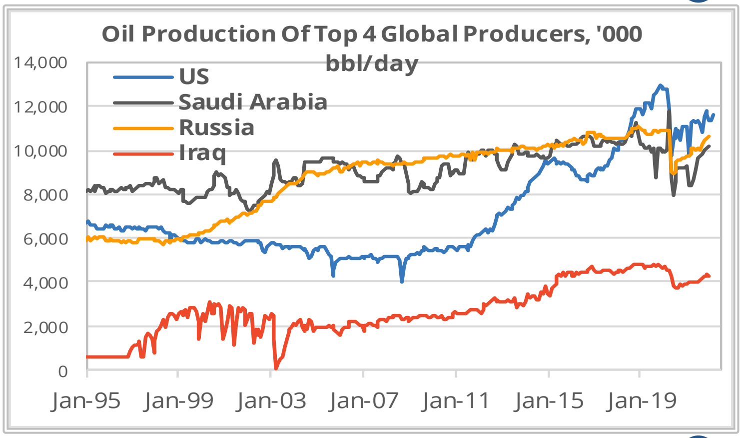
(since 1996, looking only at peaks which were followed by >10% decline in EPS estimates)



Alternative Investments

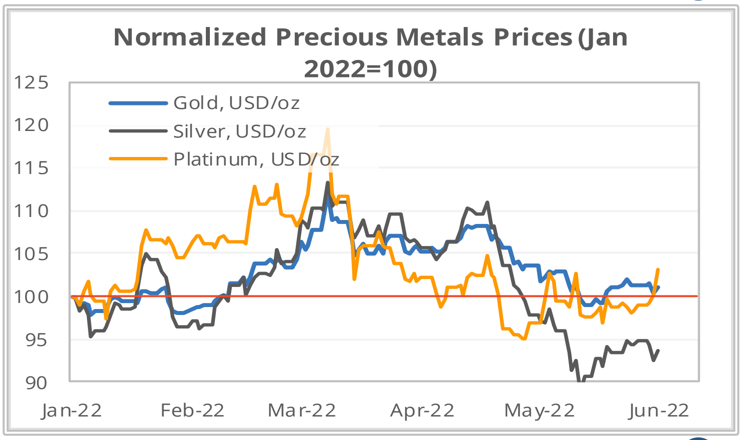
① ***Oil production continues to rebound following its steep drop in 2020, but has yet to return to pre-pandemic levels,*** and has also failed to keep pace with rising global demand. As the US heads into the driving summer season, when it typically consumes a higher amount of gasoline, the price of oil will continue to trade at historically high levels. Additional sanctions by Europe against Russian energy will also support prices moving forward.

#1



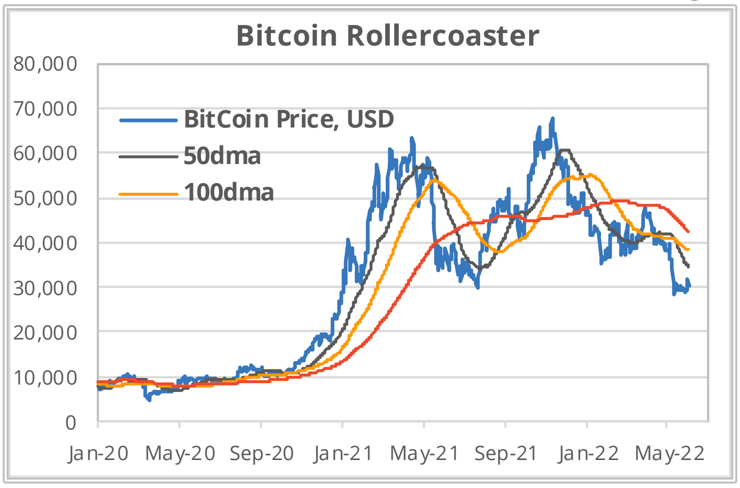
② ***We expect that traditional inflation hedges like gold, which have thus far underperformed other hedges, will see some upside*** over the coming months. This is due to the fact that 1) inflation will continue to linger at high levels, while 2) the rise in UST yields will start to level off, as most of the Fed's hiking cycle has already been priced in. As a result, the attractiveness of USTs will wane as real yields continue to be negative across all maturities, and non-yielding assets will be seen more favorably.

#2



③ ***Bitcoin has failed thus far in its role as an inflation hedge,*** dropping more than 50% even as inflation accelerated. Nevertheless, cryptocurrencies have entered the mainstream and there will be a persistent demand among many retail investors and a growing segment of institutional investors. At present prices, we believe that risks are weighted to the upside, and technical analysis suggests a fairly strong support level at the 30,000 dollar mark.

#3



Source: Bloomberg, Bulltick

As of 06/01/2022

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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