



REZCO

Rezco Webinar:
Fed Pivot Or Policy Error?

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January 2024

What Happened in December?

- The Fed pivoted to very dovish
 - On interest rates and
 - Quantitative tightening
- Rezco core view is now “no landing”
- “For Now” strong Global Equity Markets
- Expensive Equity but earnings growth will drive it up
- MM (cash) funds now heads to Equity: problems in 2025
- Fat Tail (something breaks) risks are higher

What was Rezco Positioned for?

Before Pivot

Scenario	No Landing	Soft Landing	Normal Recession	Something Breaks
Probability	10%	40%	45%	5%
Earnings Impact	5% to 15%	0% to 5%	-10% to -20%	-25% to -45%
Description	The Fed /CB has done enough to cool inflation, the market is pricing that the economy can operate with steep negative sloping yield curve, strong economic data, strong consumers and corporate earnings, high wage inflation, but declining inflation..	Inflation falls to target while wages decelerate, corporates tighten up but profits are stable and balance sheets strengthened.	The Fed/ CB's need a recession to break inflation, unemployment rises to curb wage increases, services super-core inflation is stickier and requires a recession to cool demand.	Something breaks due to: 1) impact of rapidly increased interest rates 2) geopolitical shock eg Taiwan/Ukraine/Israel/Iran and nuclear tensions etc 3) inflation remains sticky - Fed hasn't done enough 4) Bond rates blowout.

What is Rezco Positioned for?

After Fed Pivot

Scenario	No Landing	Soft Landing	Normal Recession	Something Breaks
Probability	45%	15%	15%	25%
Earnings Impact	5% to 30%	0% to 10%	-10% to -20%	-25% to -45%
Description	Fed did a major pivot and threw out everything that they have been saying about not repeating the 1970's .	Inflation falls to target while wages decelerate, corporates tighten up but profits are stable and balance sheets strengthened.	This is now deferred to 2025 The Fed/ CB's needs a recession to break inflation, unemployment rises to curb wage increases, services super-core inflation is stickier and requires a recession to cool demand.	Inflation comes back 1970's style in 2025 Something breaks due to: 1) impact of rapidly increased interest rates; or 2) geopolitical shock eg Taiwan/Ukraine/Israel/Iran and nuclear tensions

Funds Positioning (Current Holdings)

	Managed Plus	Value Trend	Stable	SA Equity	Global Flexible
SA Equity	21%	8%	5%	95%-99%	
Global Equity	37%	31%	24%		60%
Total Equity	58%	39%	29%		60%
SA Gov Bonds (R186)	19%	23%	19%		
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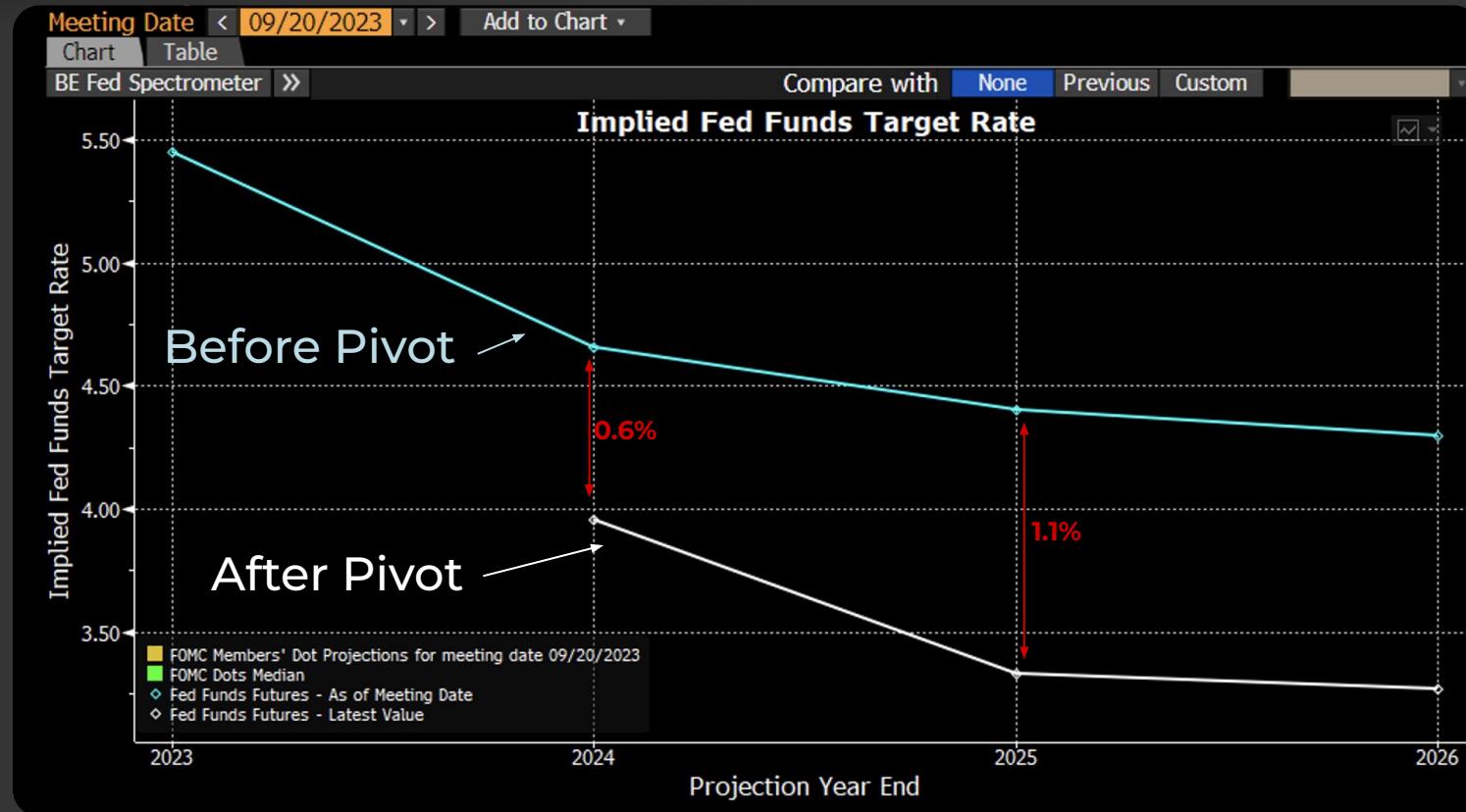


The Great Fed Pivot

The Great Fed Pivot Sep 23 Vs Dec 23



Market Pricing of the Rate Cuts



The Pivot

September Meeting

- Fed expecting one more hike before year end

November Meeting Verbiage (paraphrased)

- We are only thinking about where to stop hiking.
- Next is to think about how long we hold rates for
- Only then would we even think about when to cut

December Meeting

- Increased the 2024 interest rate cuts from 2 to 4 times
- And to stop doing QT sooner

Why the Pivot?

Option One:

- The Fed was seeing something very dark in the economy
- Some positive (lower) and surprising inflation news

Option Two:

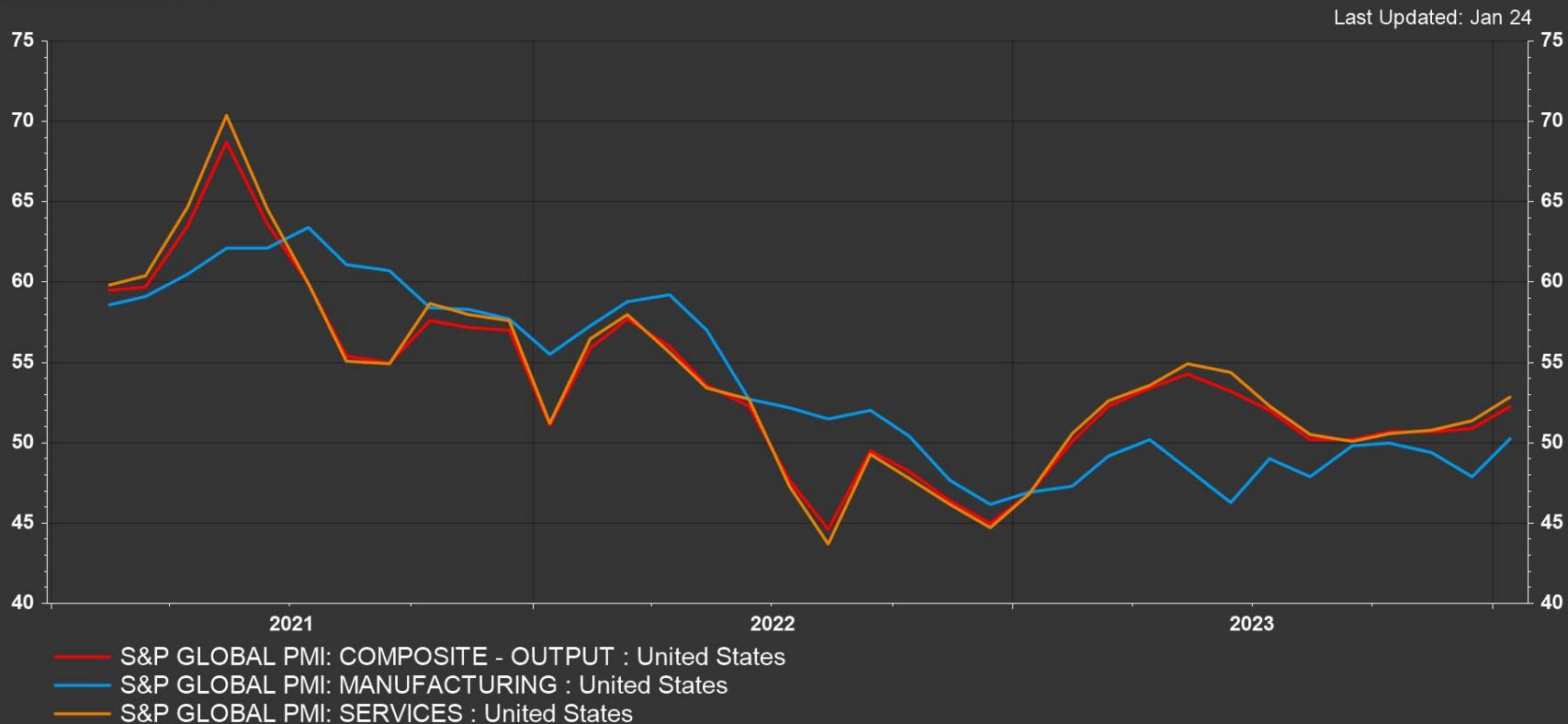
- Other Non-Economic Reasons

Super-Core Inflation: Why the Pivot?

Previously the Fed made it very clear that this is a key variable



USA PMI's: Why the pivot?

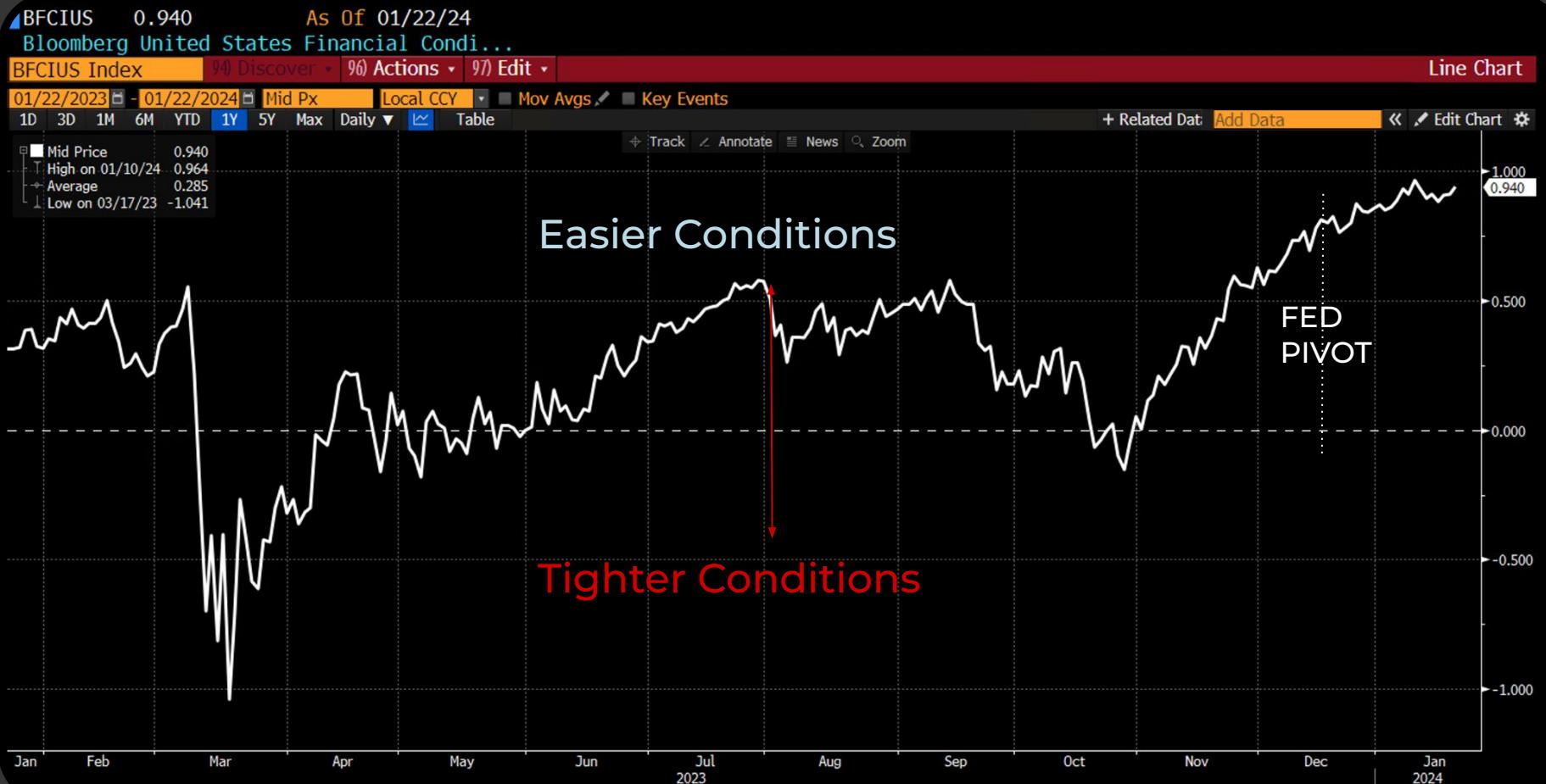


Source: LSEG Datastream / Rezco

Bloomberg Economic US Surprise Index

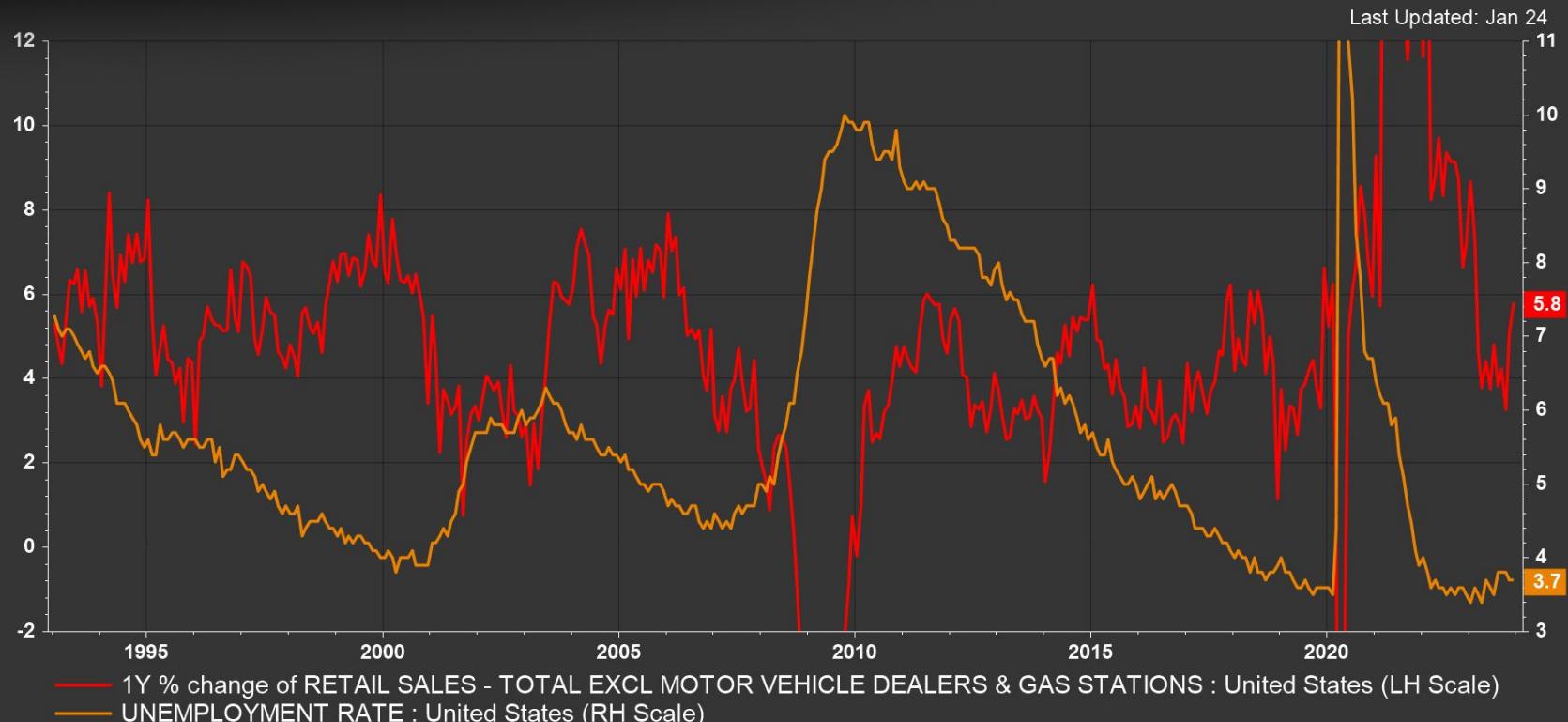


Bloomberg Financial Conditions Index

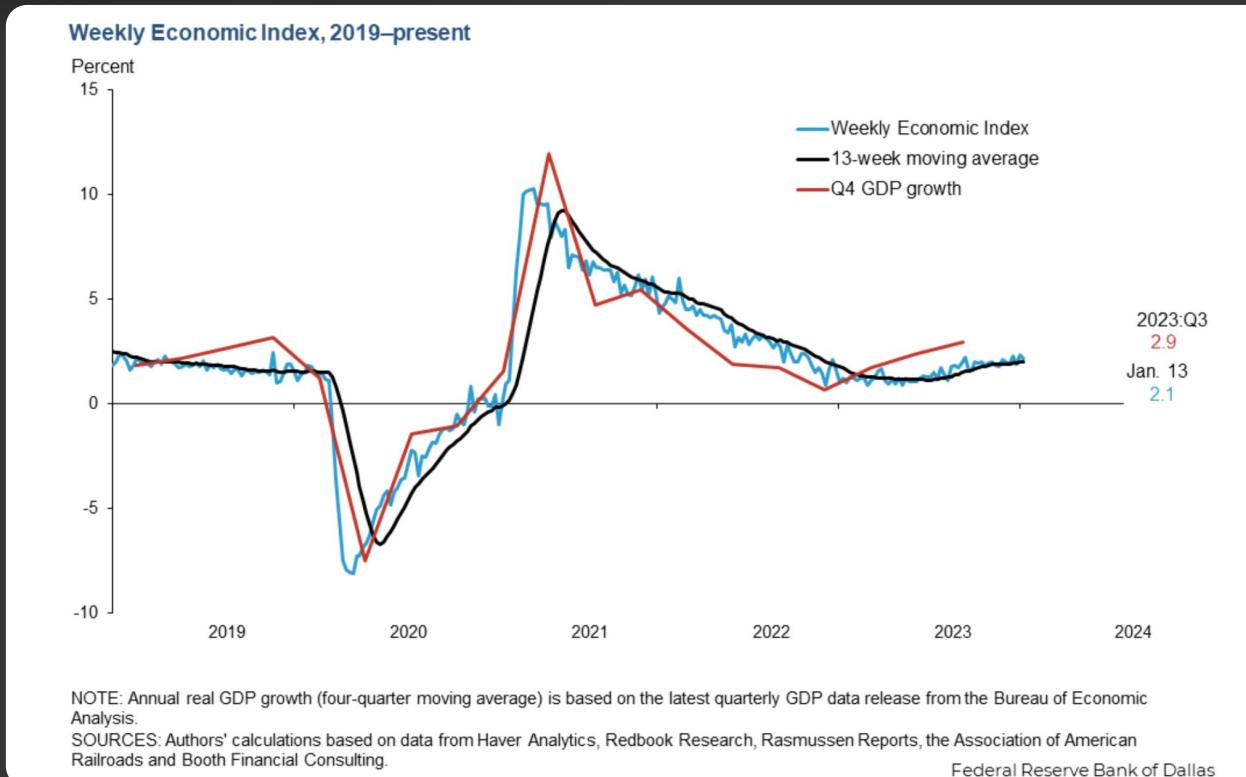


Retail Sales Accelerating:

Why the pivot?

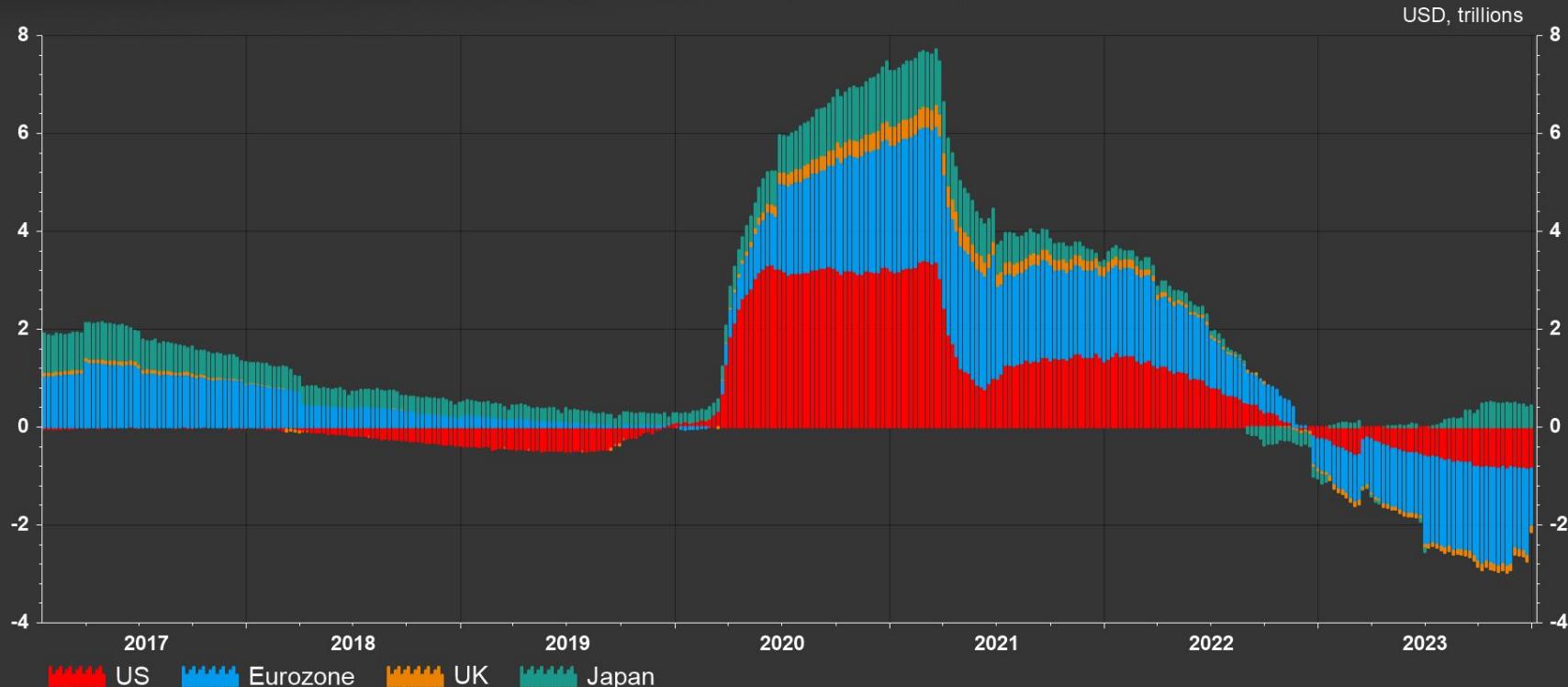


US Economy Bottomed Mid-2023?



QT - The Fed is Already Blinking

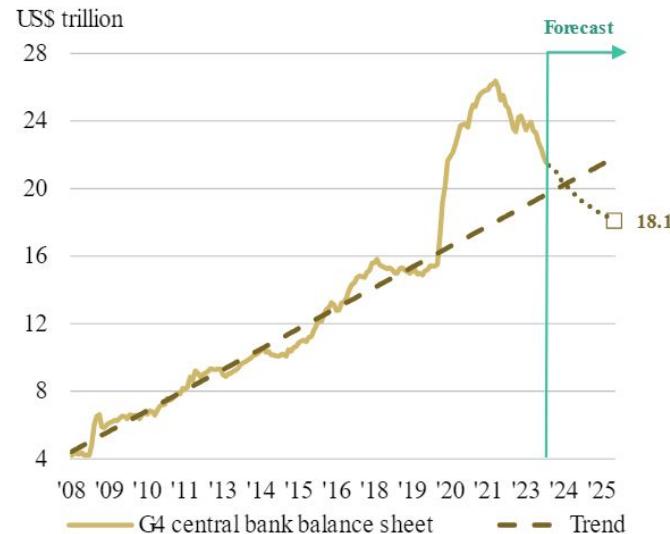
Central bank balance sheets, total assets using average exchange rate over 7 years



Source: LSEG Datastream / Rezco

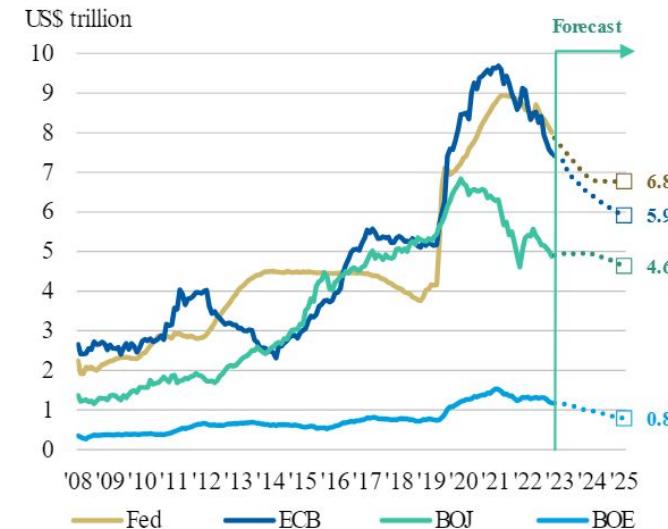
Market QT Expectations: Another \$ 2tn

Exhibit 1: G4 central bank balance sheet size, Morgan Stanley forecast, and pre-pandemic trend



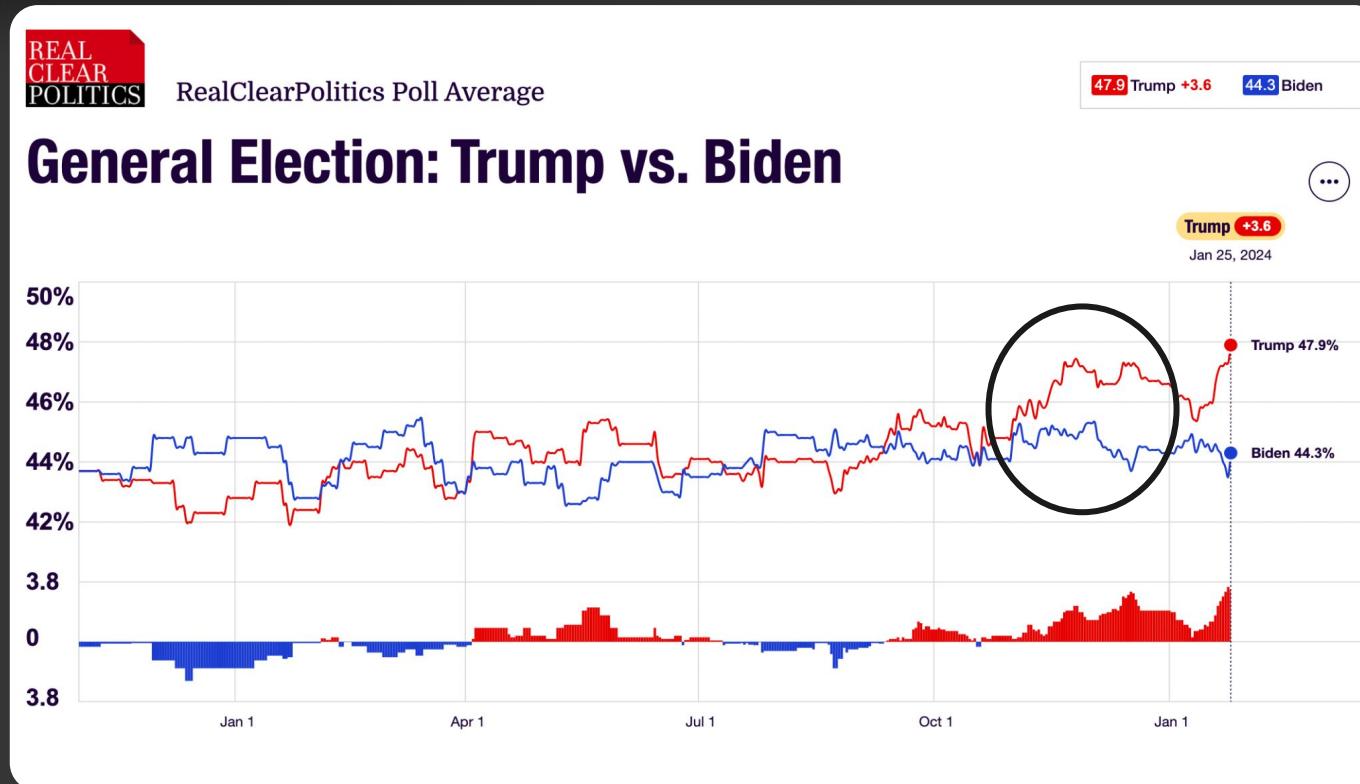
Source: Morgan Stanley Research estimates, National Central Banks, Bloomberg

Exhibit 2: Fed, ECB, BoE, and BoJ balance sheet sizes and Morgan Stanley forecast



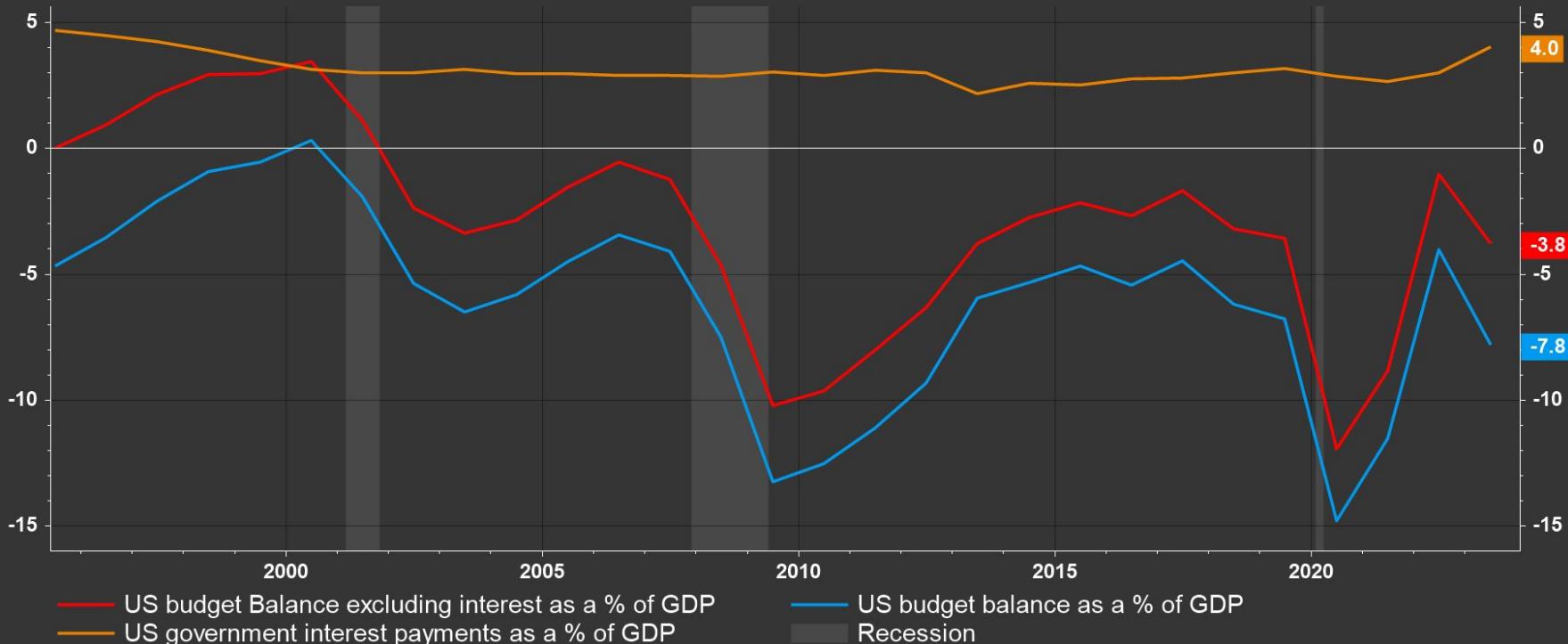
Source: Morgan Stanley Research estimates, National Central Banks, Bloomberg

Why the Pivot? Could Be:



Fiscal Stimulus Continues: US Deficit

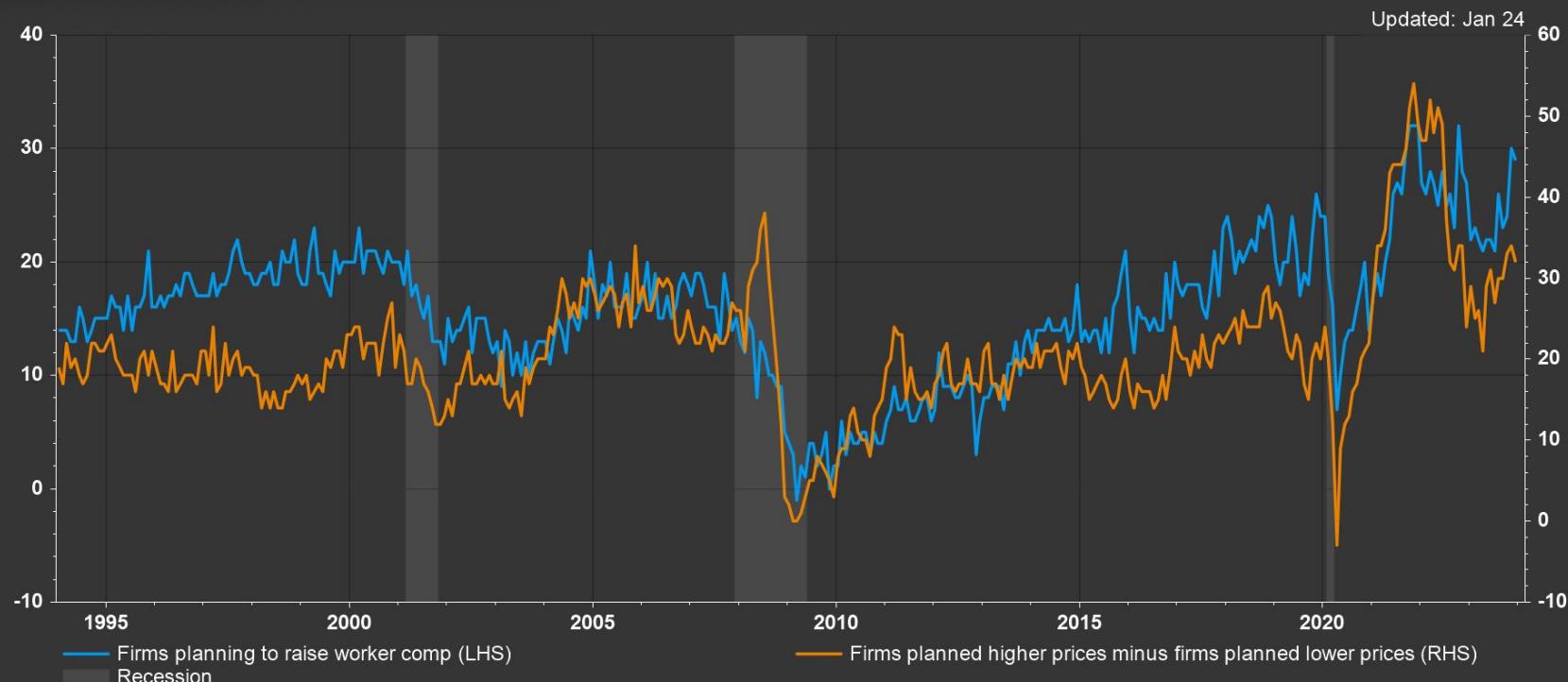
(Primary & Budget Balance) as % of GDP



Source: LSEG Datastream / Rezco

That Didn't Take Long: Firms Planning Wage & Price Increases

UNITED STATES WORKER COMPENSATION



Source: LSEG Datastream / Rezco

US Firms Raising work comp vs FED Wage Growth Tracker

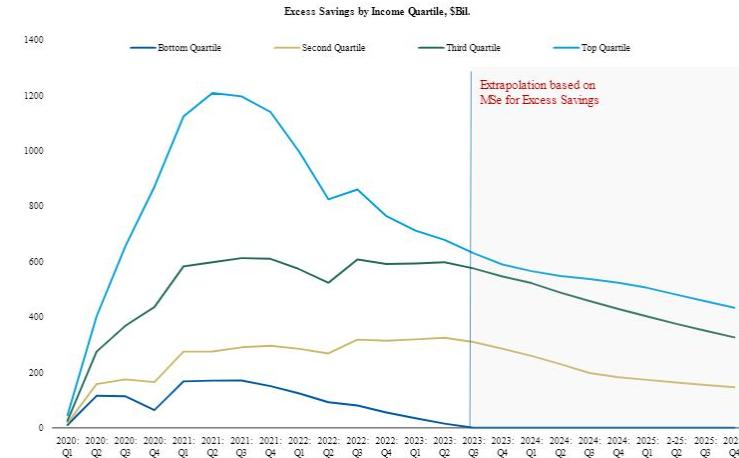


Source: LSEG Datastream / Rezco

USA Excess Savings:

The poor have spent it, the rich still have it to invest

Exhibit 88: Consumer excess savings vs pre-Covid levels continues to dwindle across all income cohorts, with the bottom quartile expected to have run out of excess cash this quarter.



Source: Federal Reserve Distributional Financial Accounts,
Morgan Stanley Economics Estimates

S&P 500 FWD Earnings Growth Vs Fed Funds Vs S&P



Market is Expensive Relative to Interest Rates, but not if Rates Fall



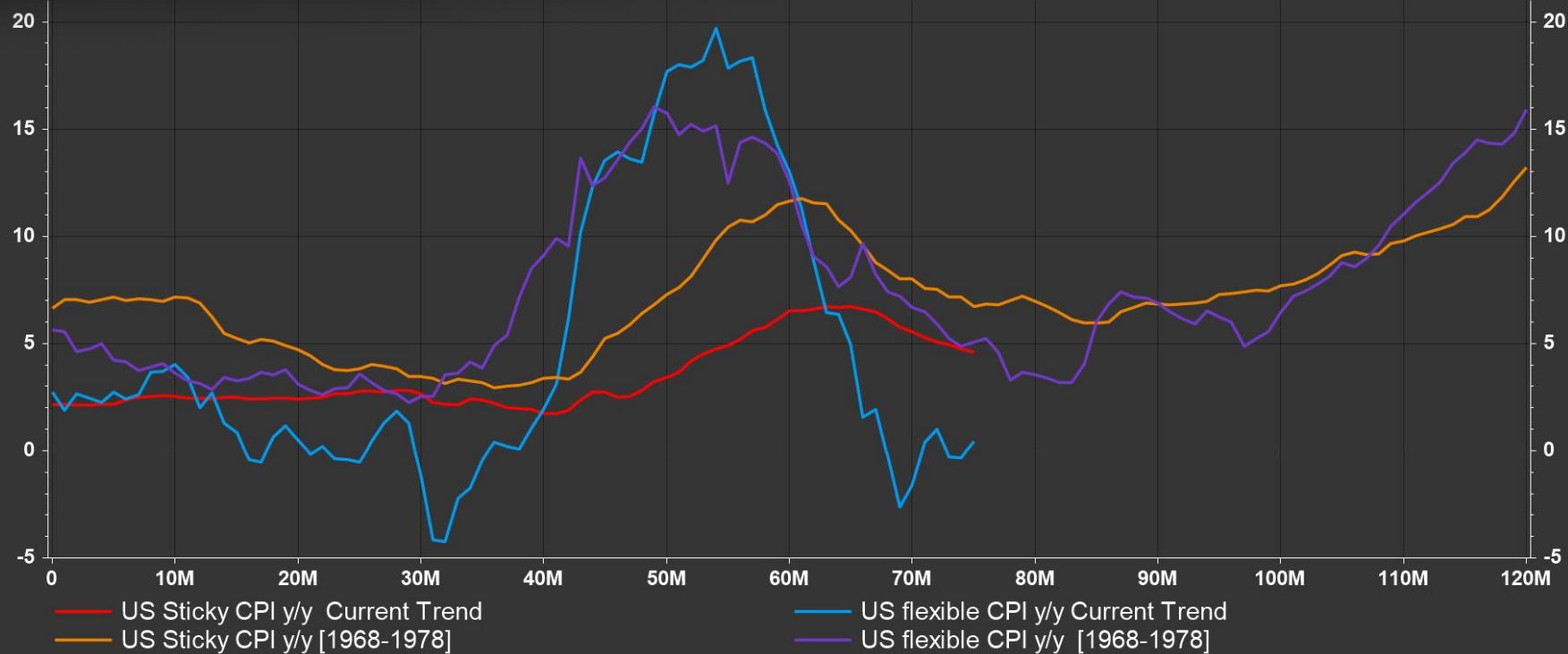
Source: LSEG Datastream / Rezco



The Risk for 2025: Revisiting the 1970's

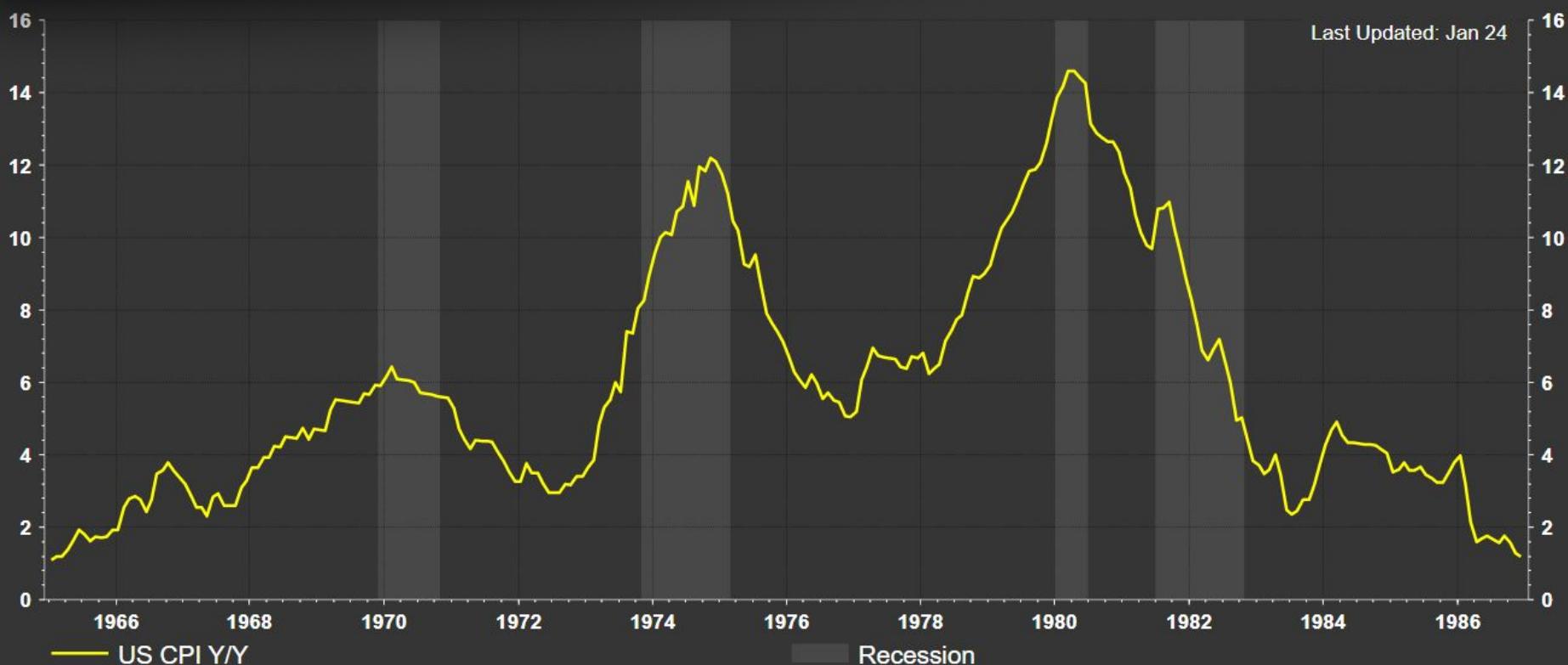
Sticky-Price CPI (1970 Vs Present)

Updated: Dec 23

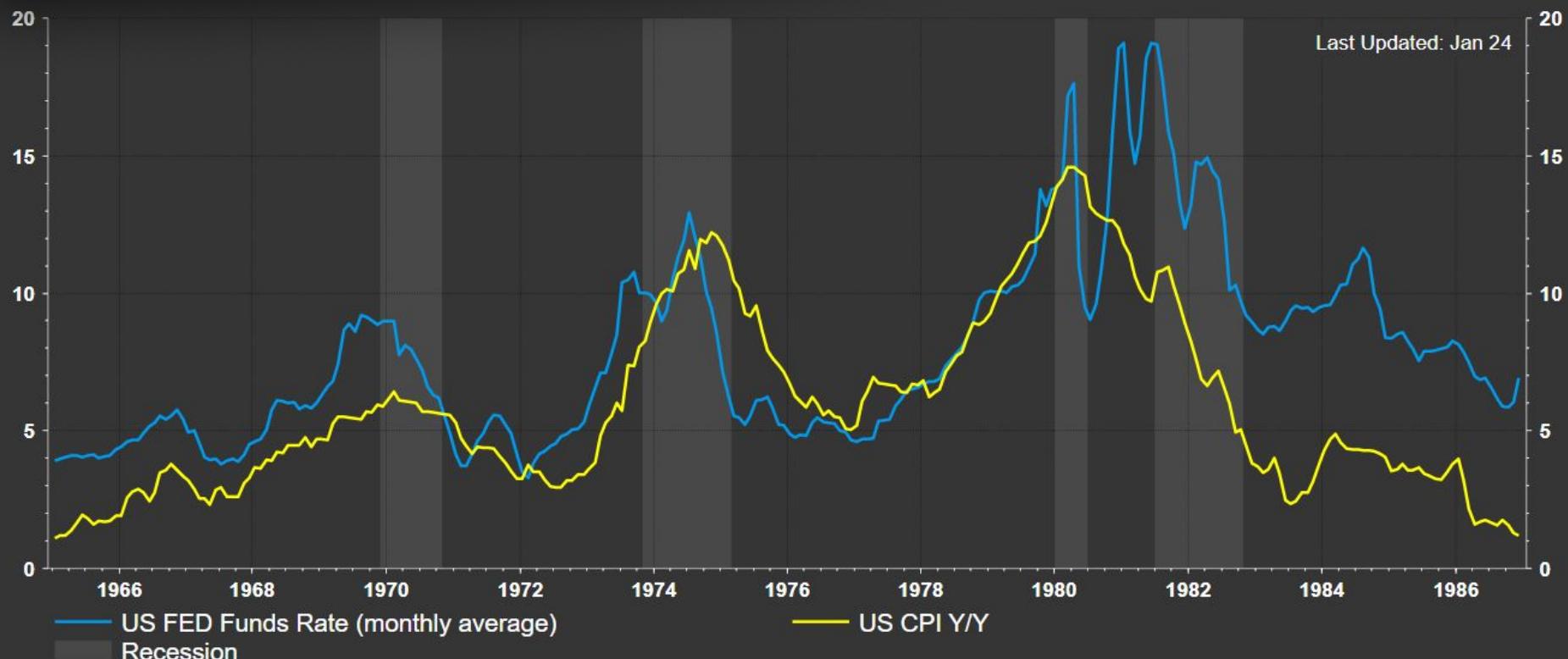


Source: LSEG Datastream / Rezco

Revisiting the 1970's: Inflation

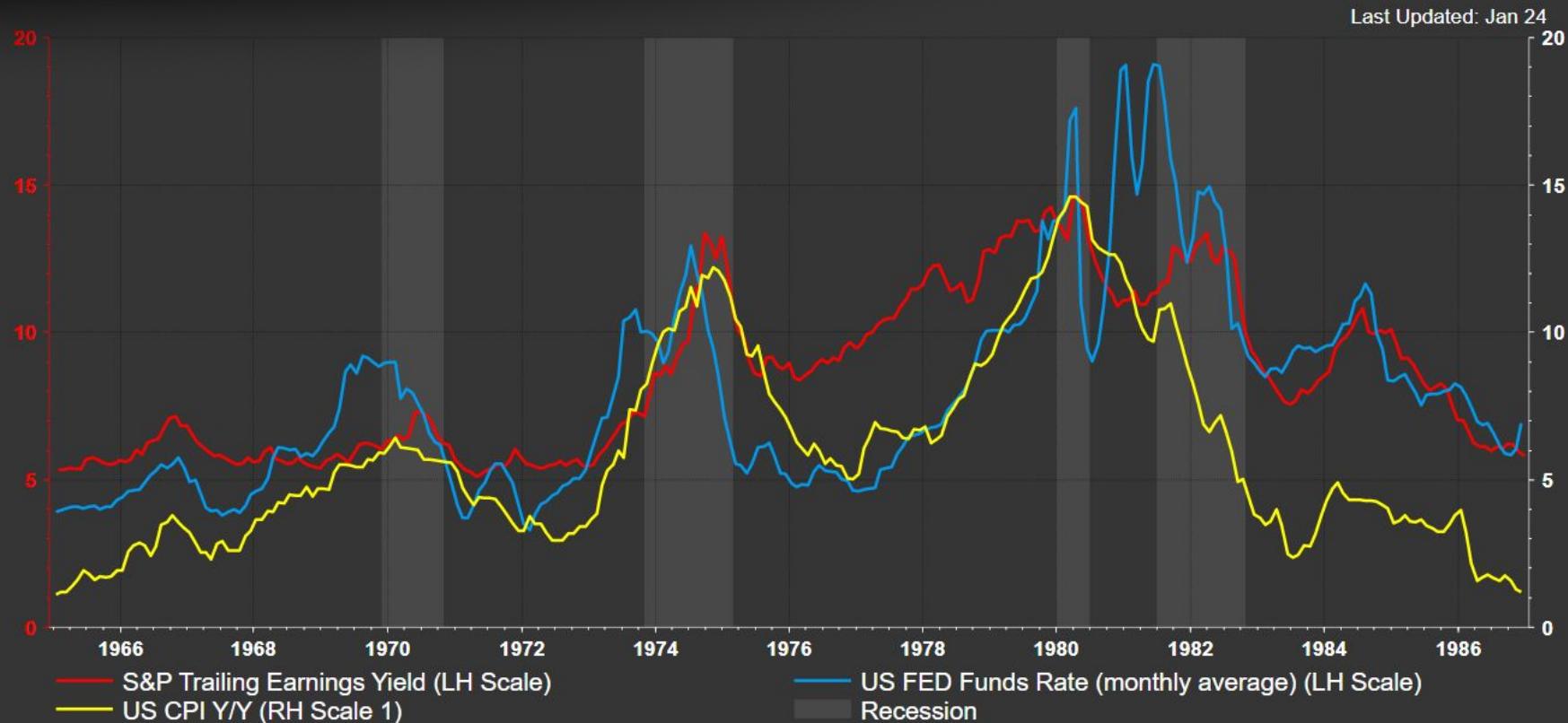


Inflation: Forced an Interest Rate Response



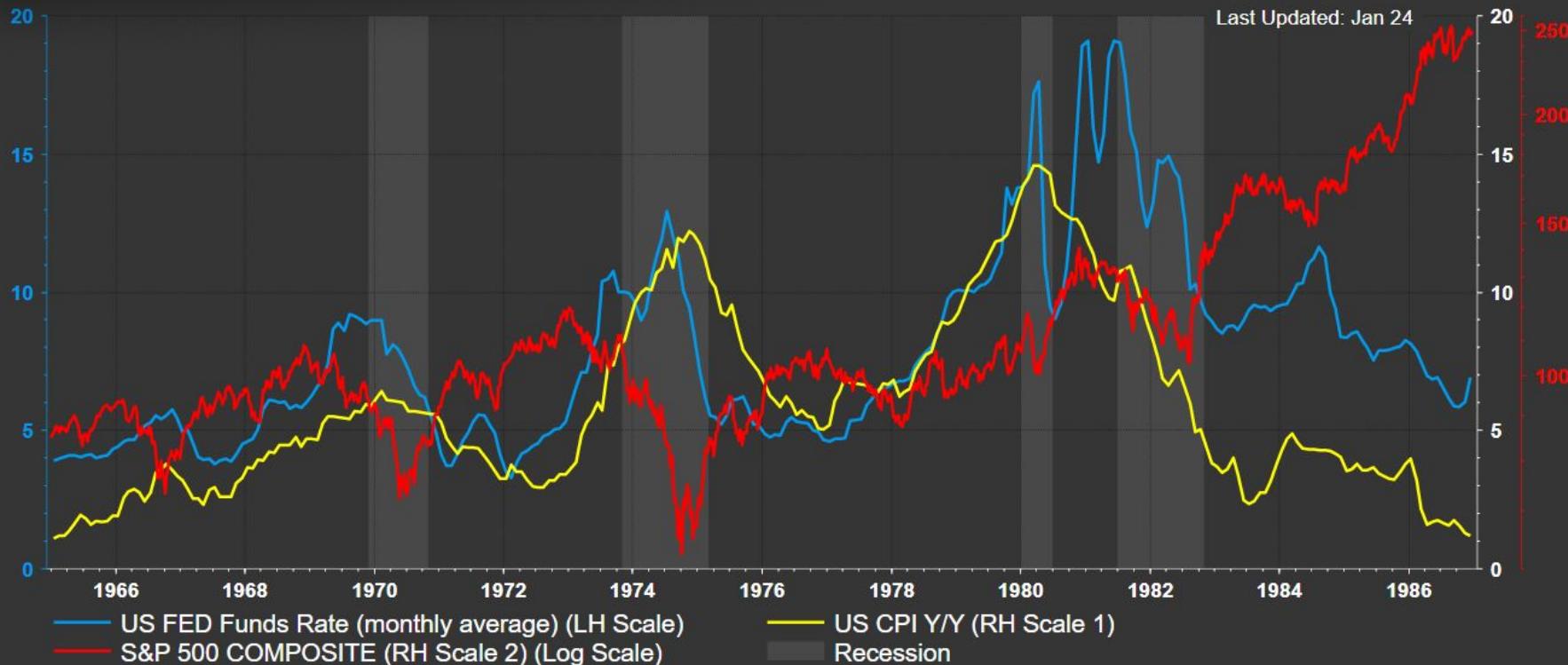
Source: LSEG Datastream / Rezco

Which Cause Earnings Yields to Rise (PEs fell)



Source: LSEG Datastream / Rezco

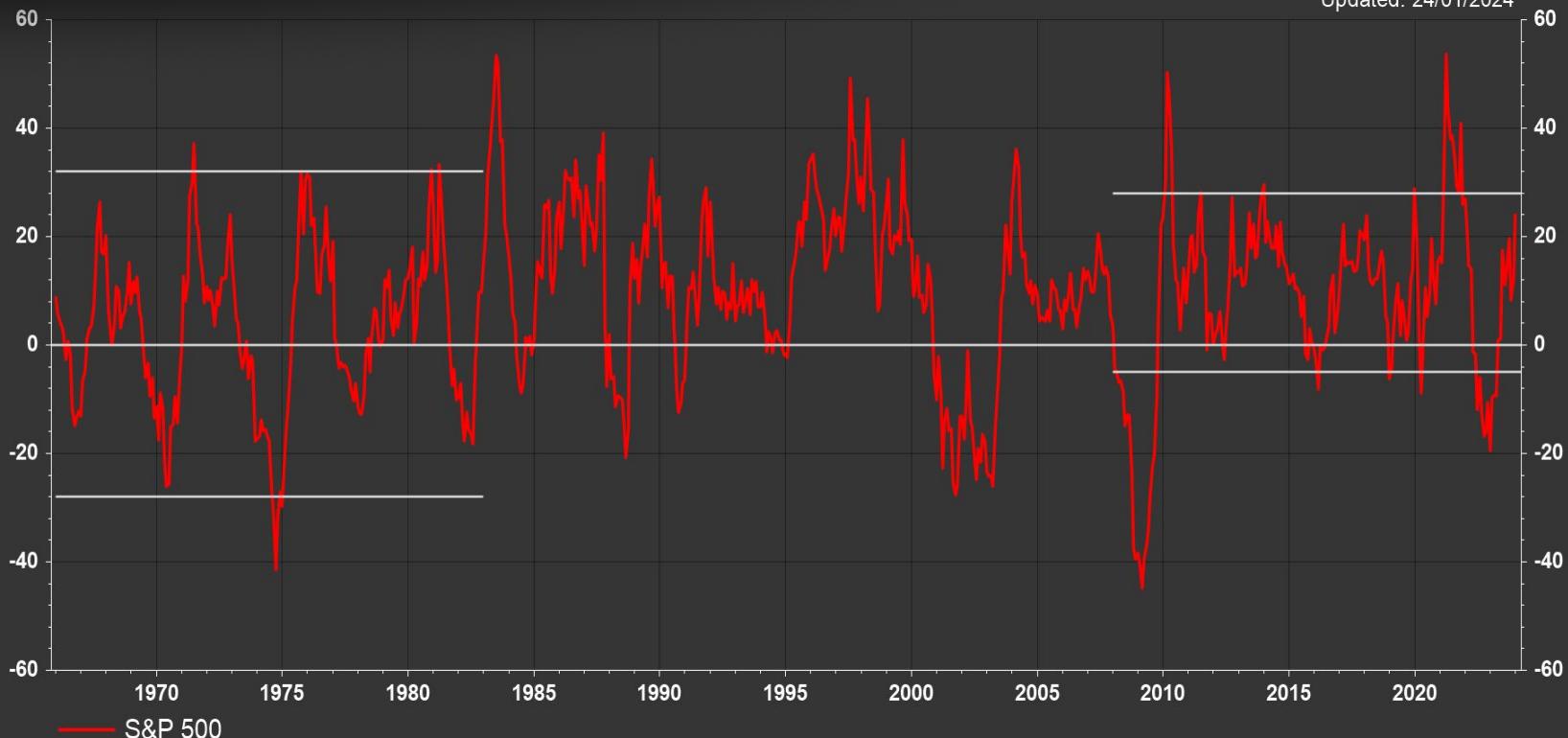
Which Really Hurt Equity Prices



Source: LSEG Datastream / Rezco

1970'S High Inflation: High Equity volatility & rolling 12 month returns

Updated: 24/01/2024



Source: LSEG Datastream / Rezco

Beware of Narratives: 1970 Vs 2020's

Nifty 50 VS Mag 7

What were the original Nifty Fifty stocks?

The Nifty Fifty was a group of 50 large-cap stocks on the New York Stock Exchange in the 1960s and 1970s, characterized by their consistent earnings growth and high P/E ratios. Examples of Nifty Fifty stocks included household names such as General Electric, Coca-Cola, and IBM.

Investopedia

The Magnificent 7 includes the following stocks:

- Apple (AAPL)
- Microsoft (MSFT)
- Alphabet (GOOG and GOOGL)
- Amazon (AMZN)
- NVIDIA (NVDA)
- Tesla (TSLA)
- Meta Platforms (META)

Jan 12, 2024

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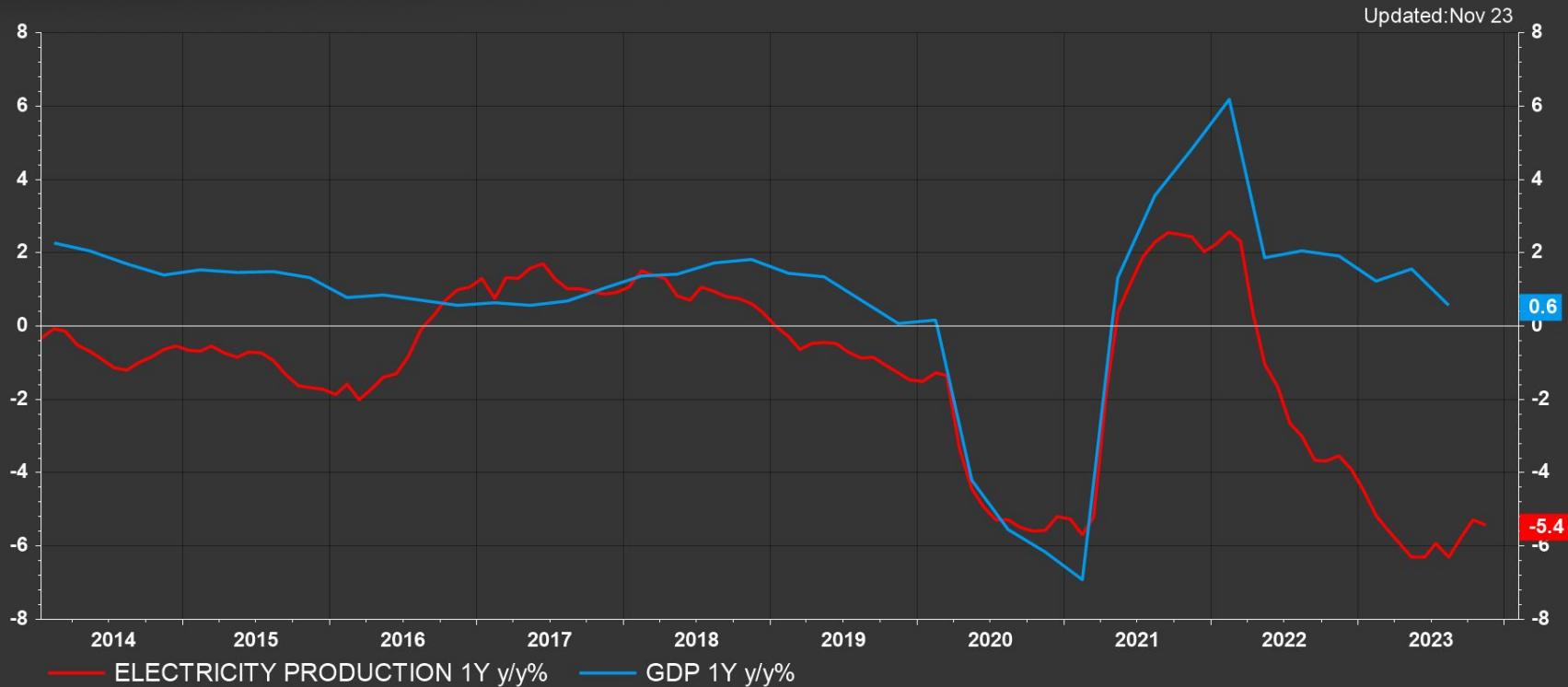
South Africa

South Africa

- Local economy stuck in low growth
- Stock picking needed to beat cash and indices
 - But be careful of illiquid shares
- ZAR stays weak with risks
- Election will be about promises

South Africa: Stuck in Low Growth

SOUTH AFRICA GDP AND ELECTRICITY



Source: LSEG Datastream / Rezco

RSA not Cheap

Given low growth & alternatives



RSA Bonds & EM Yields

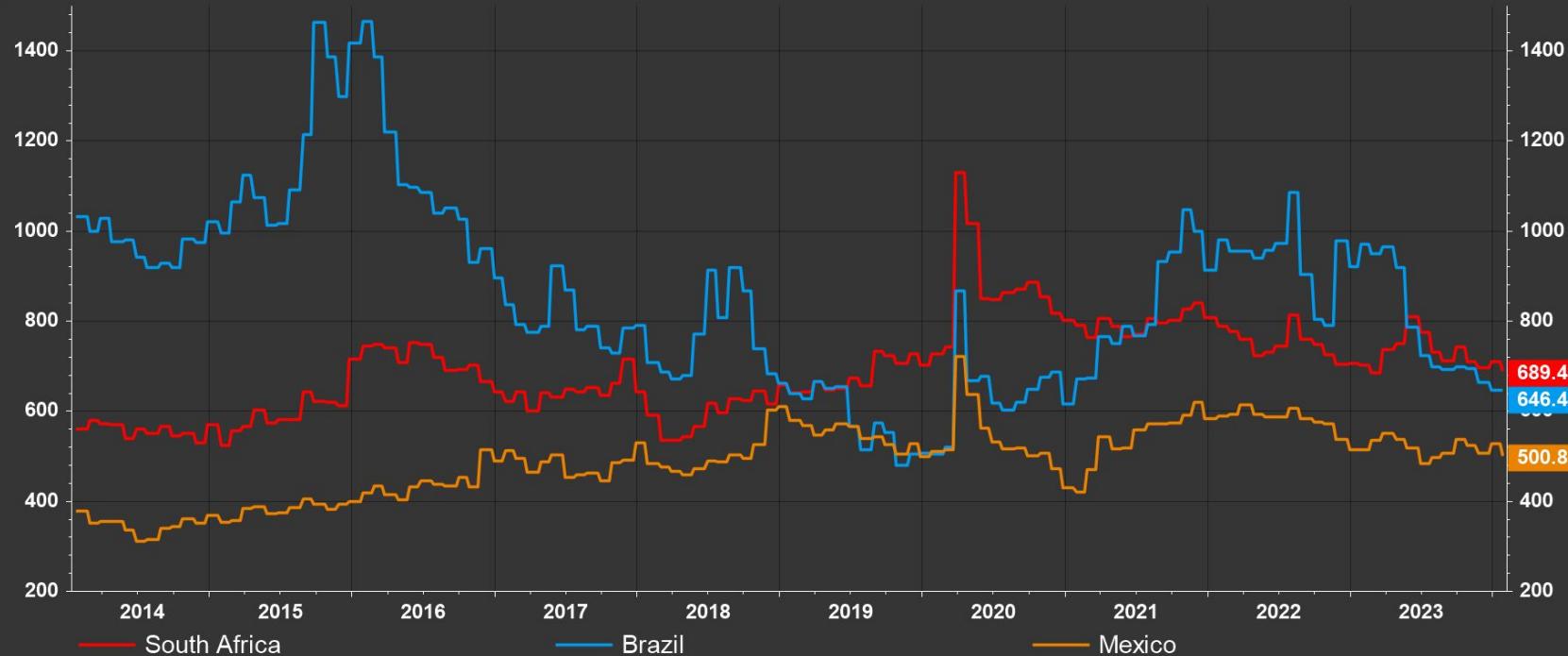


Source: LSEG Datastream / Rezco

RSA Fiscal Deterioration not Reflected in Bond Spreads Yet

EM SPREADS OVER US 10Y (LONG-TERM)

Updated: 25/01/2024

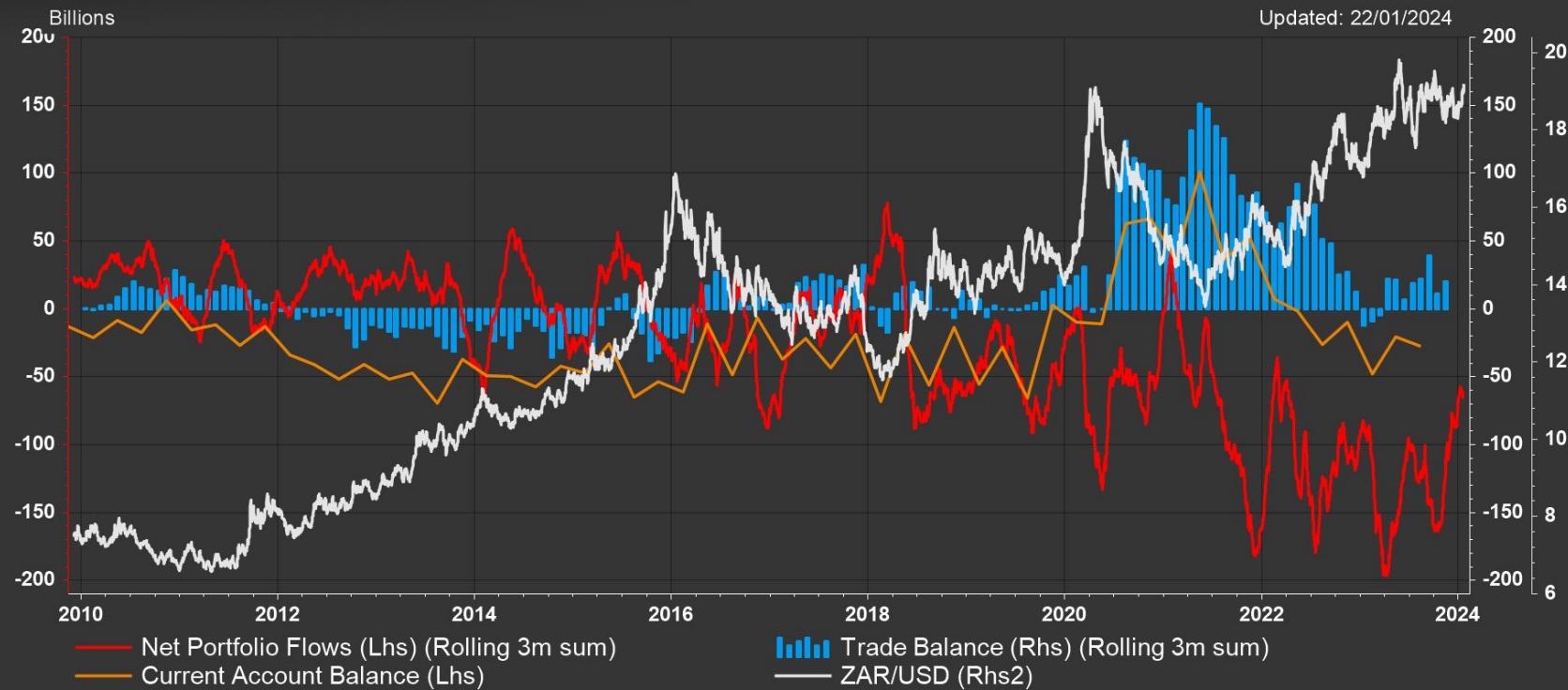


Source: LSEG Datastream / Rezco

RSA Fundamentals Point to a Weaker ZAR

Current Account Deficit and Poor Policy

SA TRADE BALANCE



Source: LSEG Datastream / Rezco



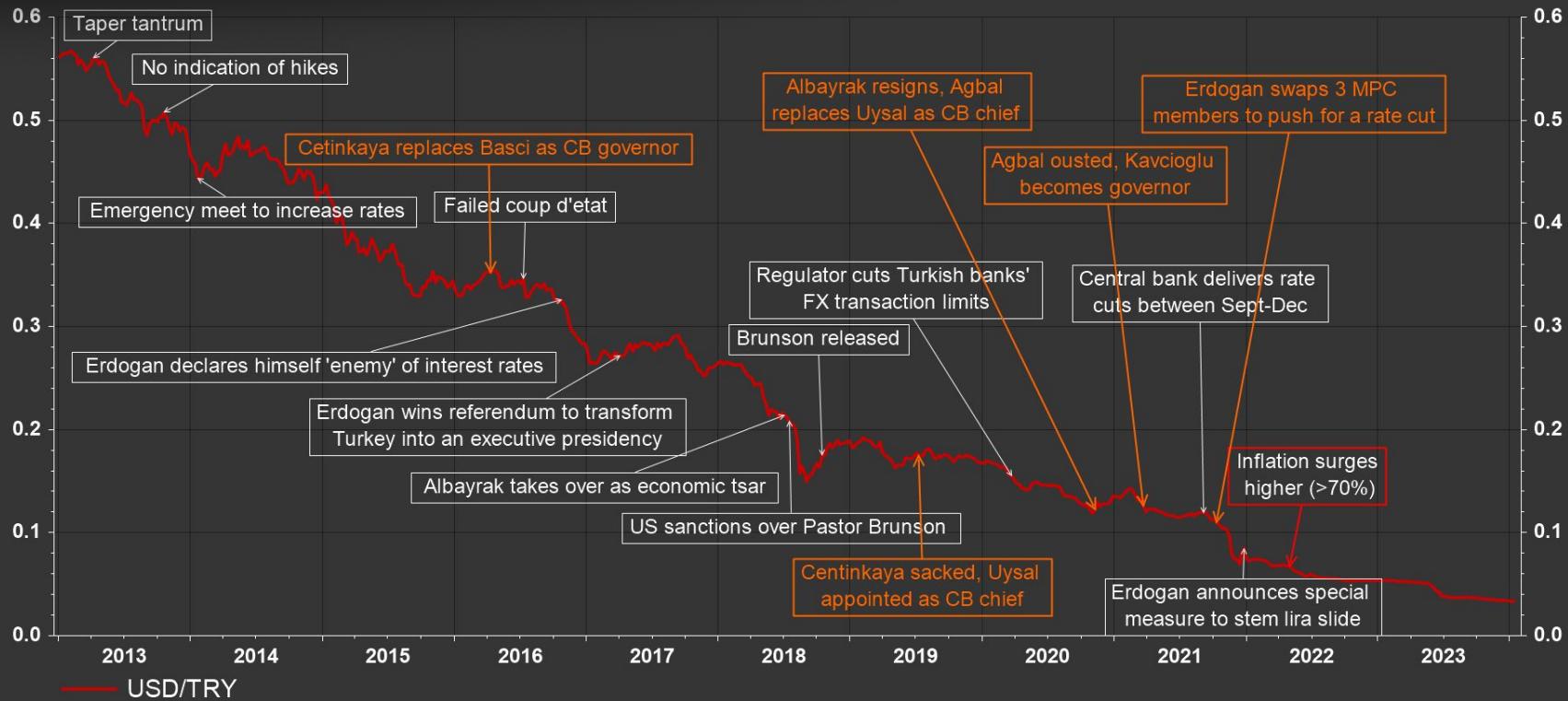
South Africa: The Turkey Scenario

Note: This is the Grey Rhino

NOT the Base Case

Identify, Observe, & React if it Charges

Impact of Contentious Policy is Cumulative



Source: LSEG Datastream / Rezco

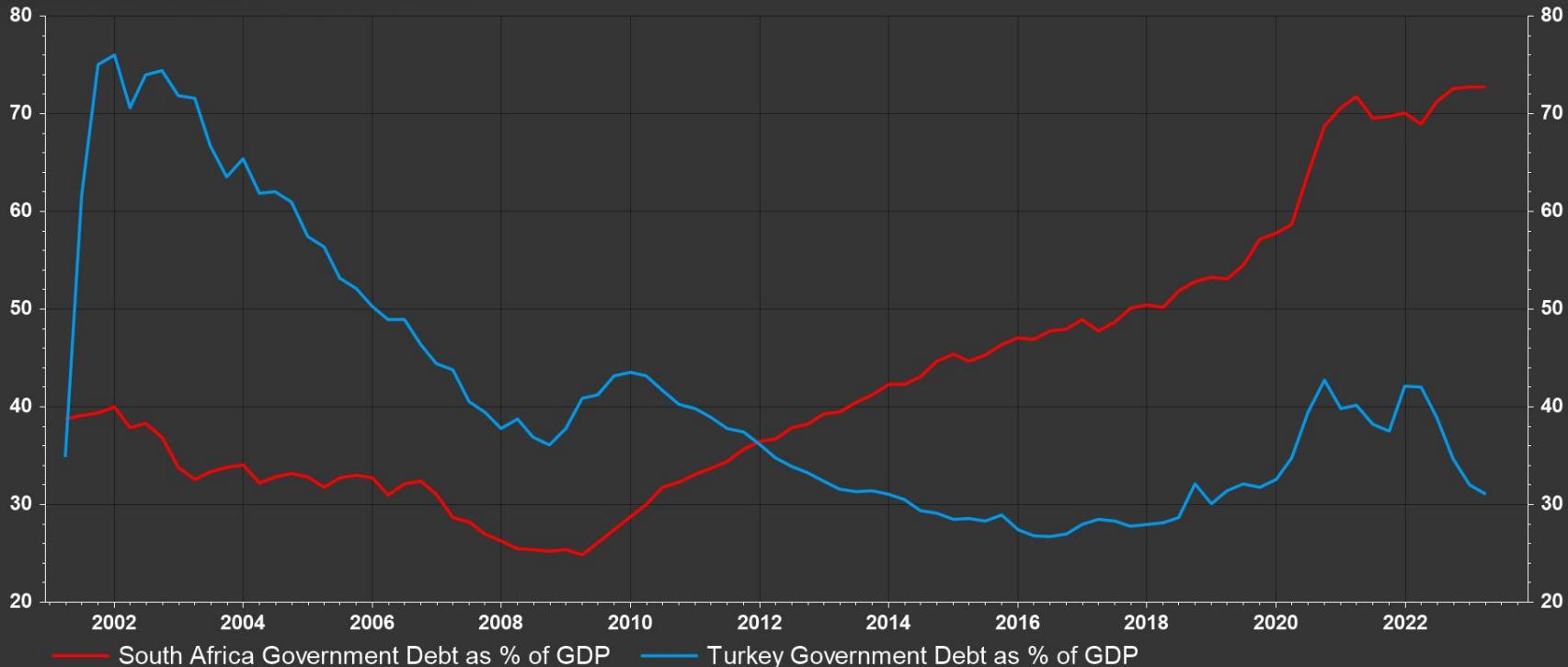
Government (ANC) - Policy Risks

- Using domestically populist foreign policy to distract from local failings.
- Getting caught in the middle in major global events
- Starting the road to non-orthodox monetary policy
- Dipping into Forex reserves
- Uncontrolled budget deficits
- Broken SOE's : No real plan to fix them

South Africa & Turkey: Debt to GDP

Government Debt to GDP (Quarterly)

Updated: Q4 23



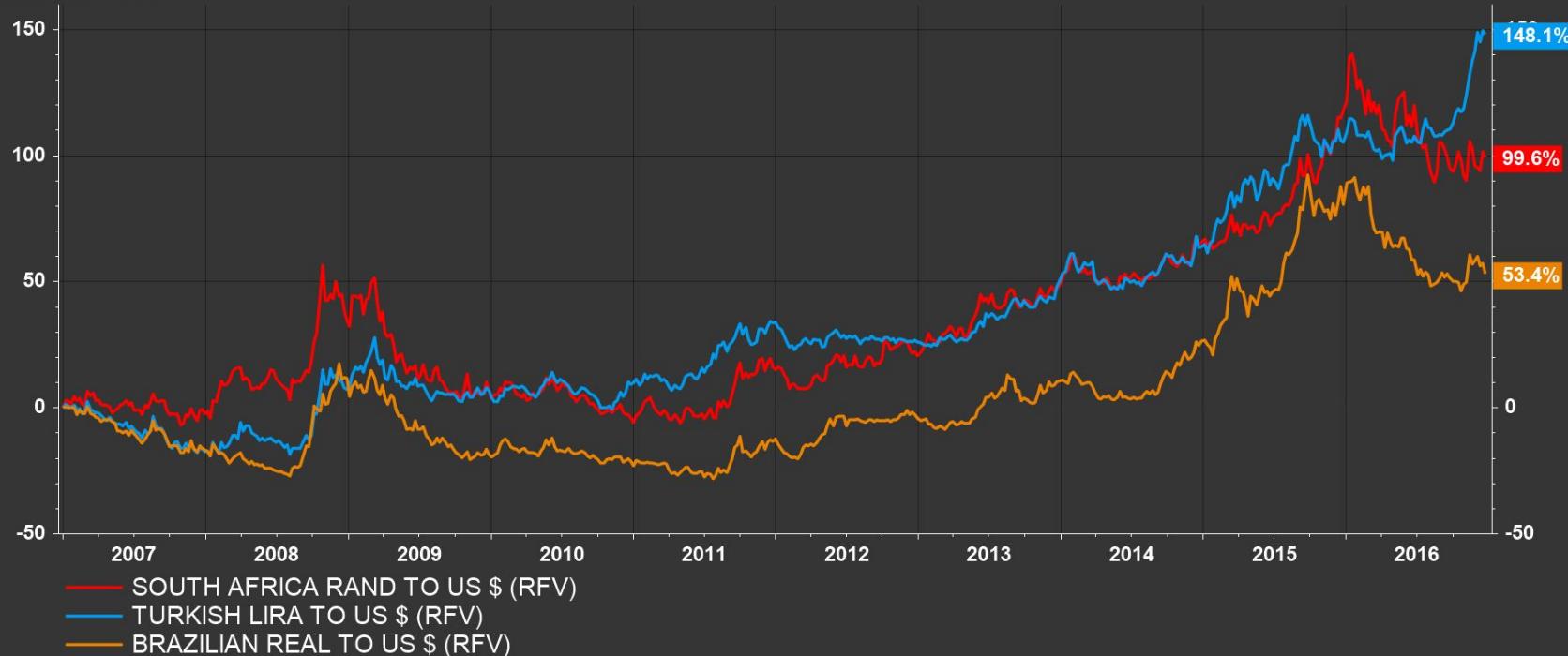
Source: LSEG Datastream / Rezco

South Africa, Brazil & Turkey

3 sibling EM's 2007 - 2017

EM Currencies vs USD [2007 - 2017]

Last Updated: 22/01/2024



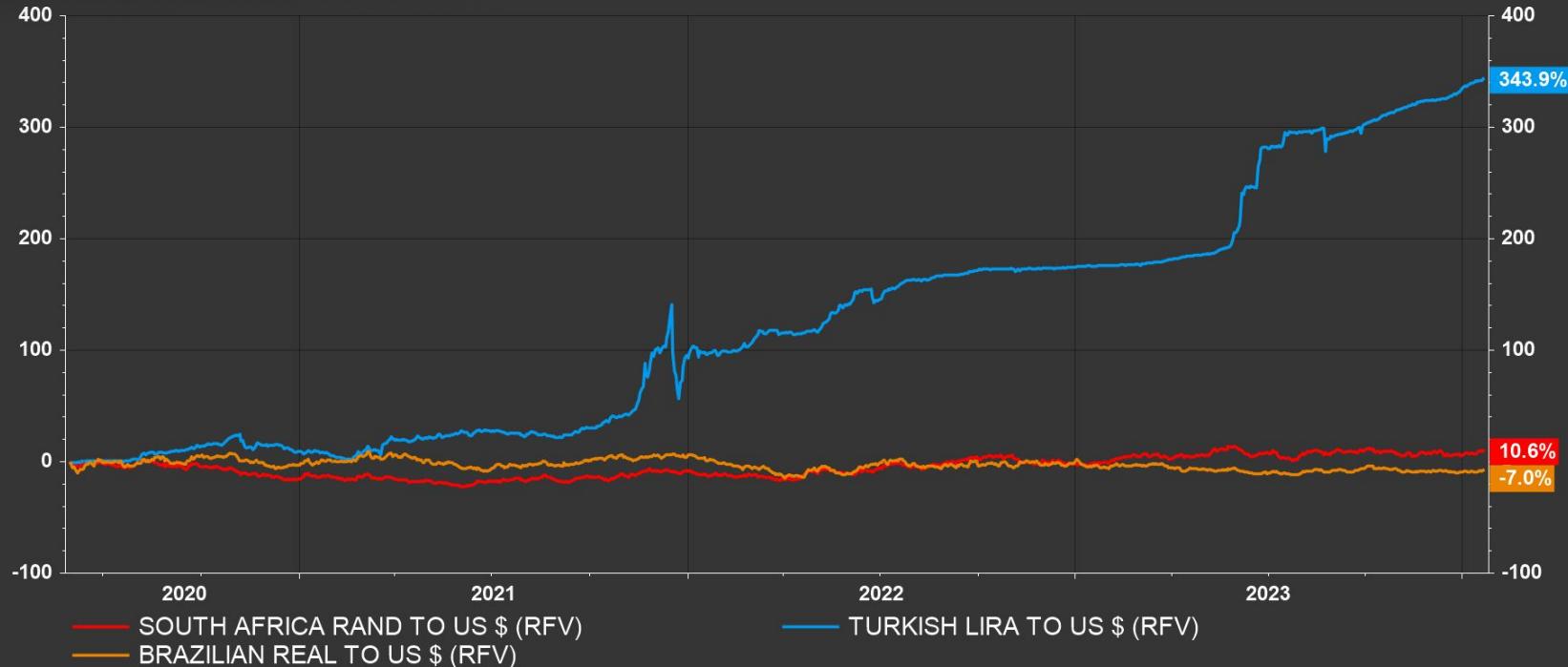
Source: LSEG Datastream / Rezco

South Africa, Brazil & Turkey

Currency & contentious policy

EM Currencies vs USD (Short-term)

Updated: 22/01/2024

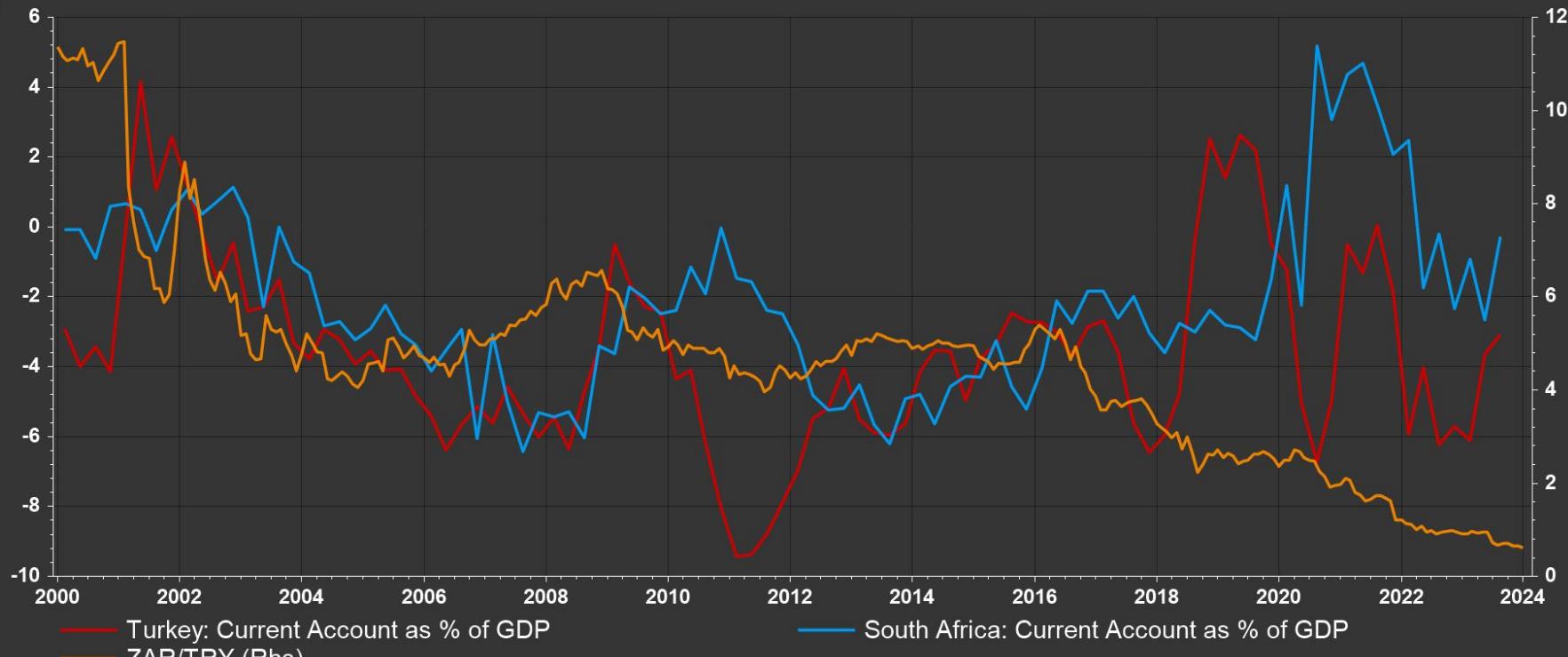


Source: LSEG Datastream / Rezco

The Grey Rhino

RSA & Turkey currency & current account

Current Account as % of GDP (Quarterly)



Source: LSEG Datastream / Rezco



Performance & Positioning Update:

Funds Positioning (26 Jan 2024)

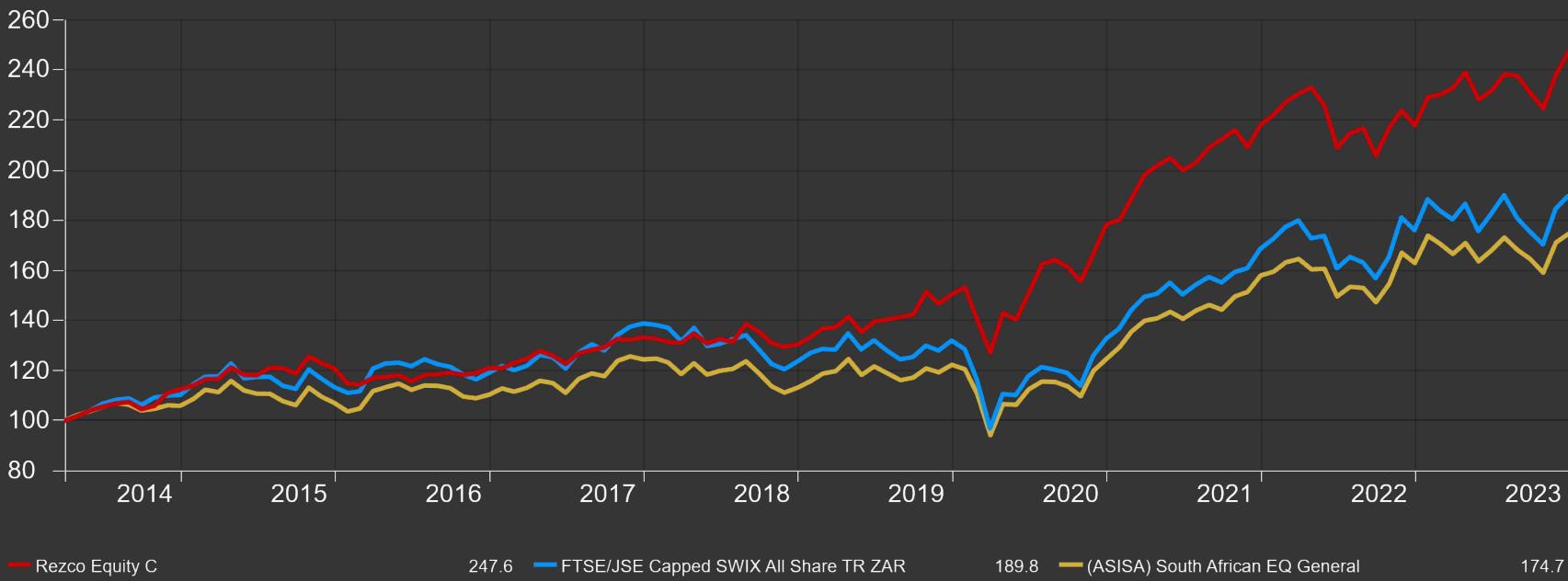
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Rezco (SA) Equity Fund

Cumulative Return Vs Peers & Capped Swix

Time Period: Since Common Inception (4/1/2014) to 12/31/2023

Currency: South African Rand Source Data: Total Return



Source: Morningstar Direct

RSA Equity: Hard Year to Beat Cash

Time Period: 01/01/2023 to 31/12/2023

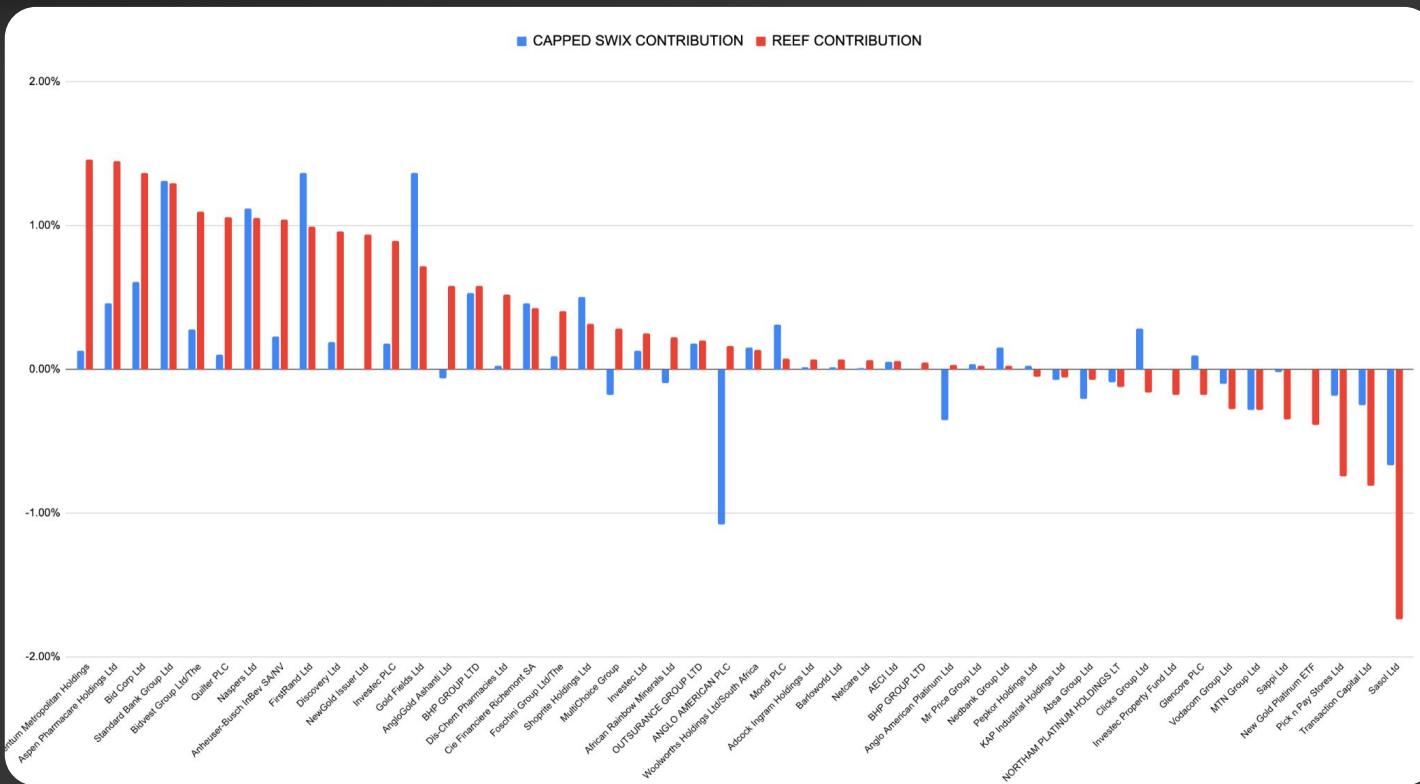
Currency: South African Rand Source Data: Total Return



Source: Morningstar Direct

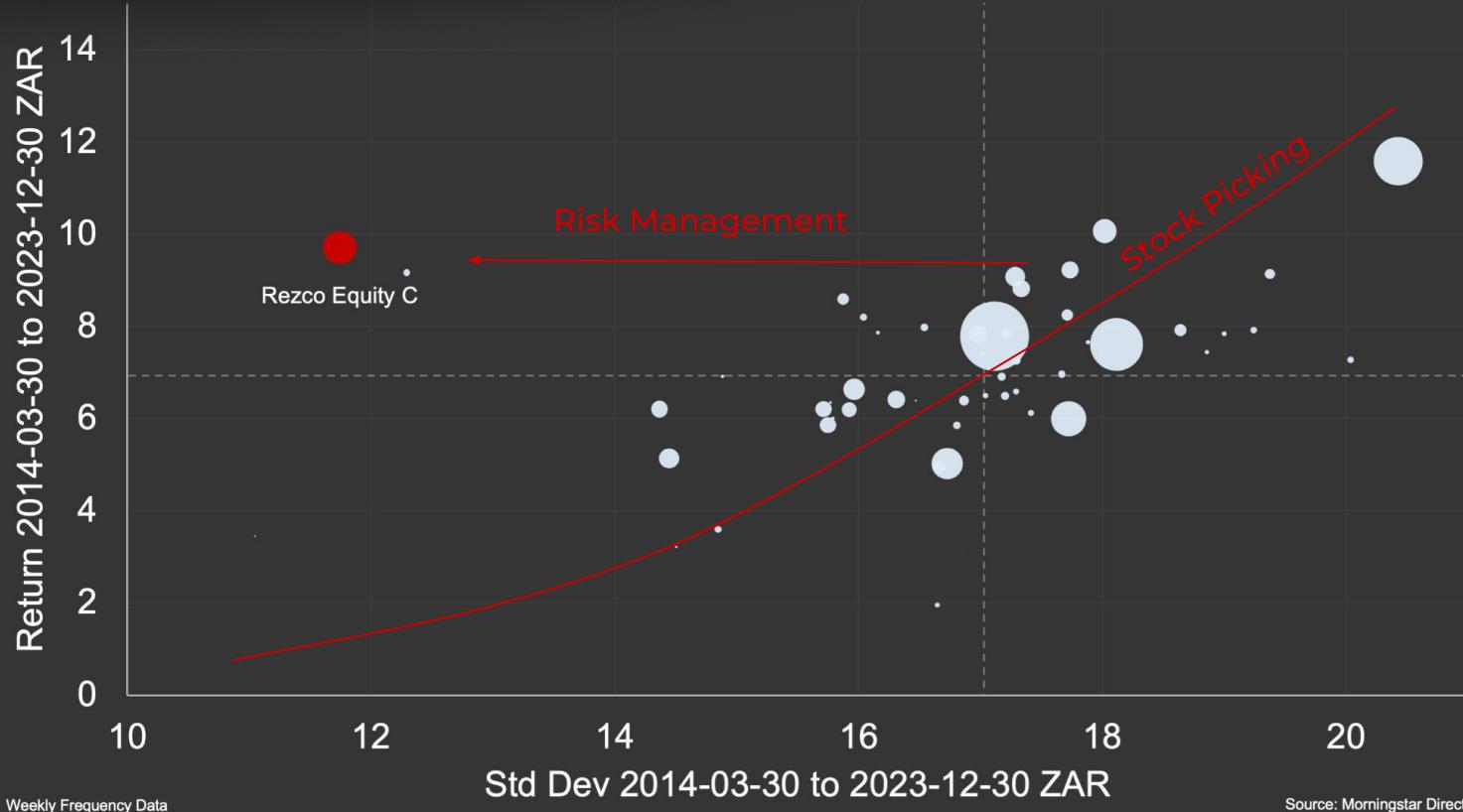
RSA Equity: Current Environment is Tough

Rezco RSA Equity Fund attribution: contributors & detractors



Risk Management the Differentiator

Funds in the ASISA SA Equity General SA only

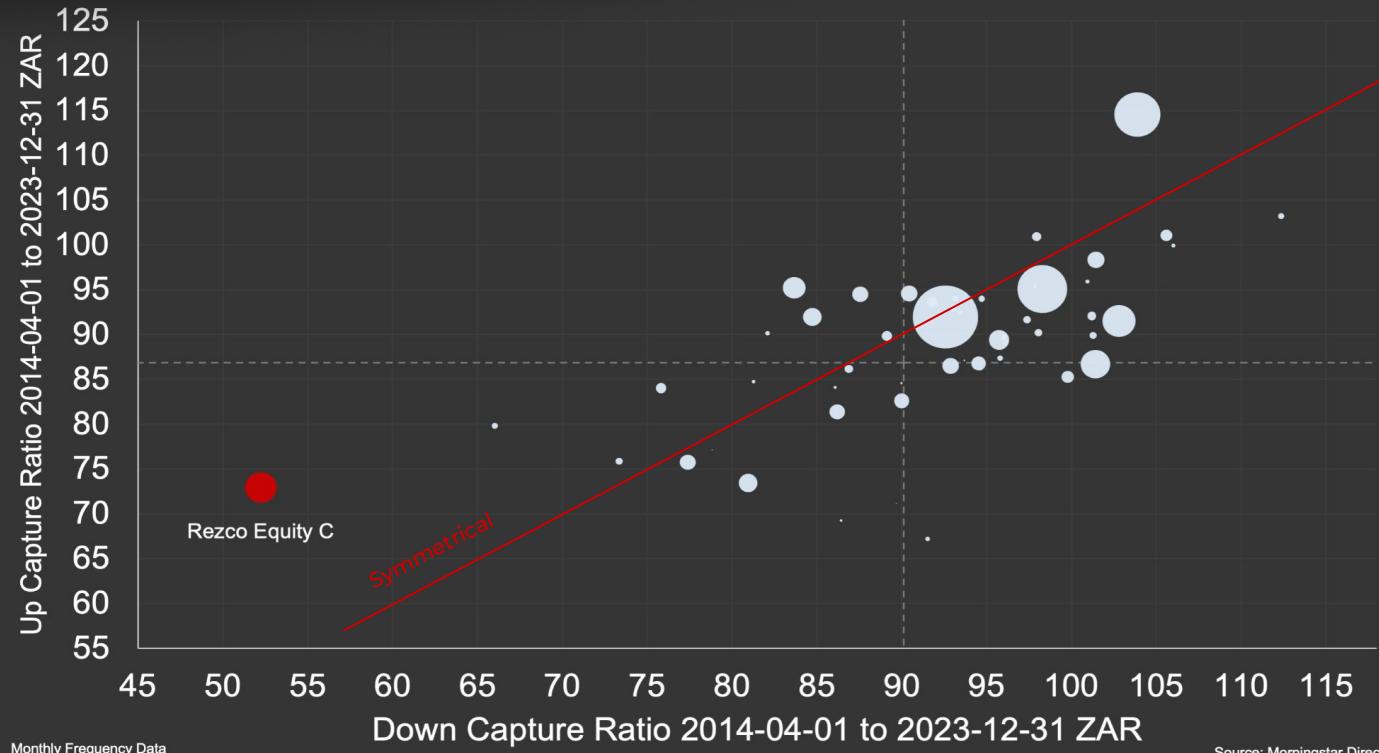


Weekly Frequency Data

Source: Morningstar Direct

Rezco Equity Fund

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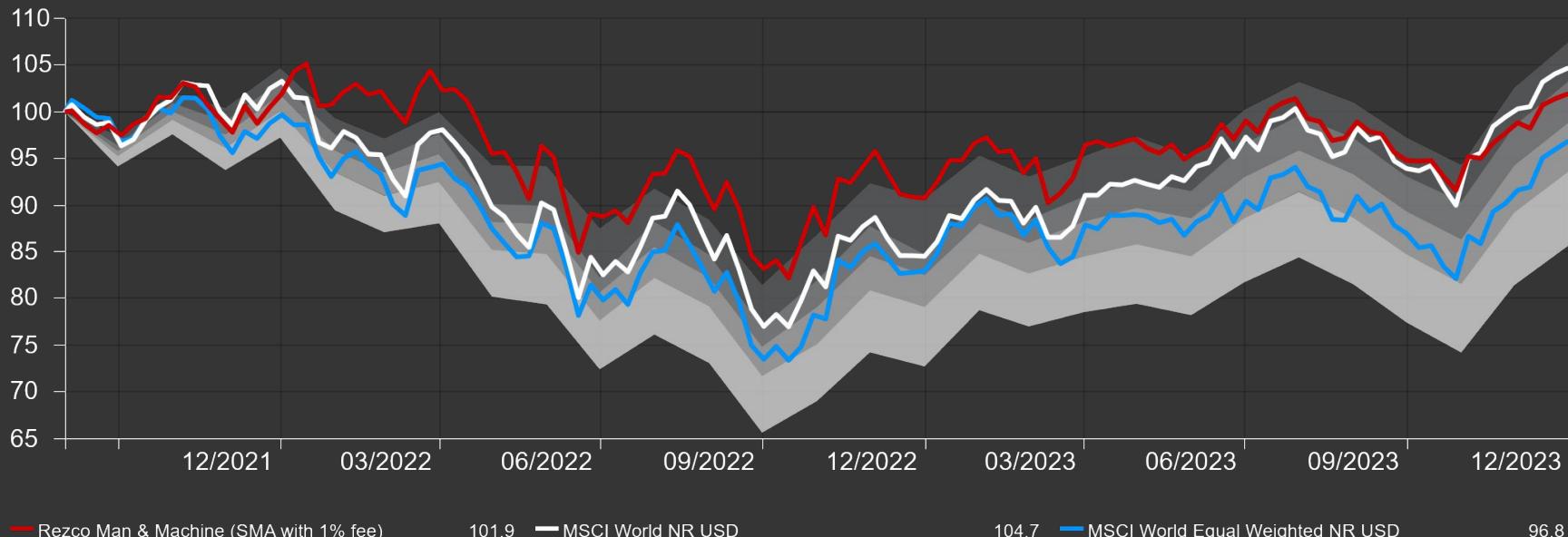


Rezco's Man Machine (SEG Mandate)

Time Period: 01/09/2021 to 31/12/2023

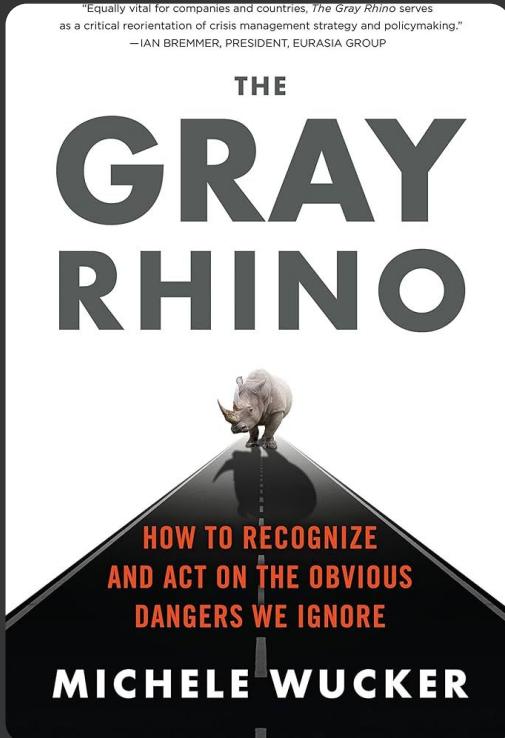
Peer Group (5-95%): Funds - Europe/Africa/Asia - Global Large-Cap Blend Equity Currency: US Dollar Source Data: Total Return

Top Quartile 2nd Quartile 3rd Quartile Bottom Quartile



Source: Morningstar Direct

Grey Rhino's



"Equally vital for companies and countries, *The Gray Rhino* serves as a critical reorientation of crisis management strategy and policymaking."

—IAN BREMMER, PRESIDENT, EURASIA GROUP

“A **grey rhino** is a “highly probable, high impact yet neglected threat...

Grey rhinos are not random surprises, but occur after a series of warnings and visible evidence.”

Key Grey Rhinos to Watch out for

Don't panic or ignore: react if they get closer

South Africa

- Monetary and fiscal policy becomes populist
- Negative consequences of foreign policy
- Messy election
- Risks of the ZAR doing a Turkey become elevated
- Solution: Max global & rand hedges in local Equity

Global

- USA signs of inflation returning
- Solution: Move to cash

Funds Positioning

Current holdings

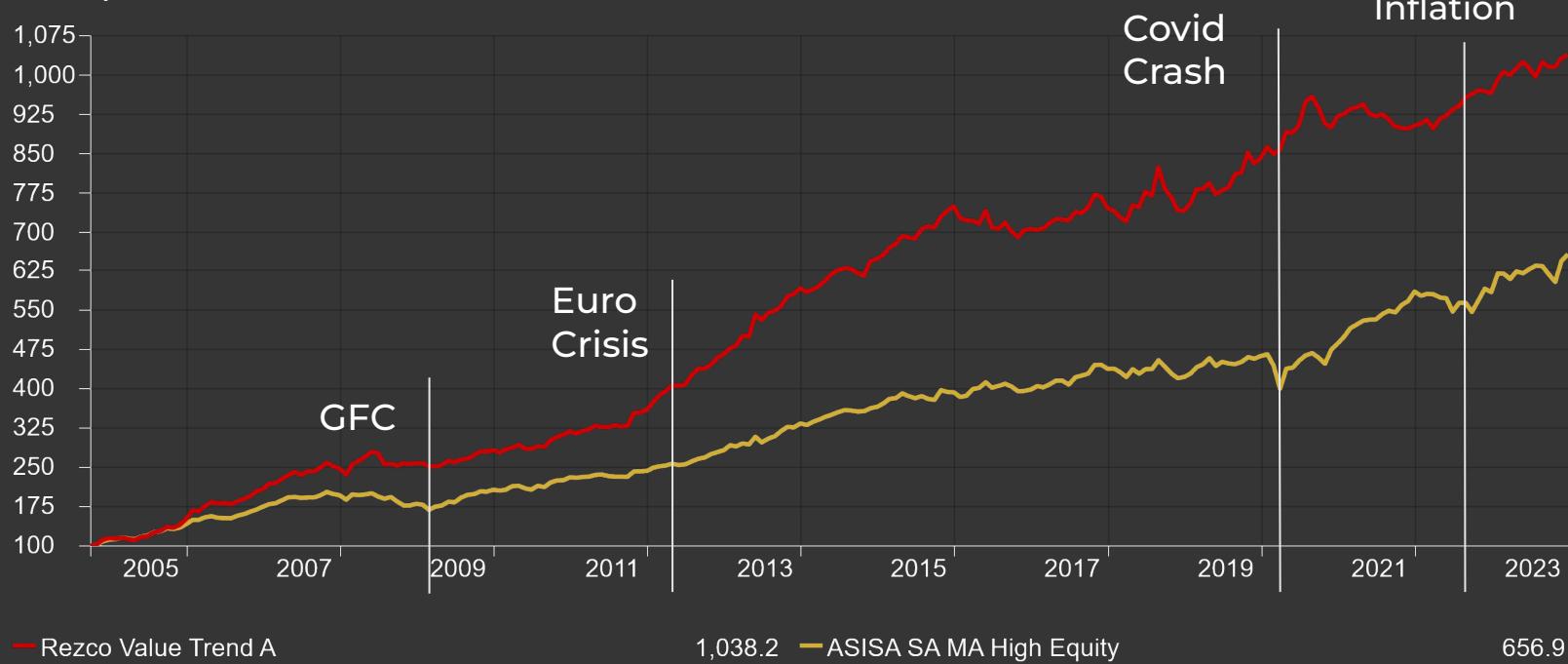
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Rezco Value Trend Vs Peers

Time Period: Since Common Inception (01/10/2004) to 31/12/2023

Currency: South African Rand

Source Data: Total Return



Source: Morningstar Direct

REZCO

Thank You



Disclaimer

Preserving Capital* & Creating Wealth.

*While the portfolio manager will attempt to minimise risk, it is possible that the investor could incur losses, including the loss of principal invested.

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