BlueLine
ASSET MANAGEMENT

MONTHLY LETTER I **February** 2020

Returns. The Blue Alpha Fund posted a negative performance in February with 57 bps coming from rates, -141 bps from equities and -14 bps on fx. Cash and costs added -1 bps.

International. The foreign scenario has proved to be quite challenging in the beginning of 2020. After the risks related to the trade war had died down, the year began with an unexpected conflict between the USA and Iran. However, this event was not enough to stop markets in their still quite positive route. This was undoubtedly supported by the notion that the world was in the midst of a recovery of growth, especially in the manufacturing sector. At the same time, the market began to monitor the electoral process in the United States, with the development of the Democratic primaries, which also did not have any great influence on the upward trend of US stock markets. The coronavirus outbreak seemed to be the third issue of the year that would not affect the positive market trend. That view proved to be wrong, since the spread of the disease to other parts of the world ended up raising major concerns regarding global growth, given its impact on demand, through channel trust, and on supply, in affecting the supply chain. We have reached the conclusion that the coronavirus is, in its essence, a transitory event, but that due to the impact on both demand and supply, it has been the trigger for the fall in global stock markets, which were already weak in terms of valuation. Looking ahead, markets will now be looking out for the moment that the virus is contained, and also for the arsenal of monetary and fiscal policies that governments will be mobilizing to support the global economy.

Brazil. The Brazilian economy was already showing some signs of economic weakness even before the coronavirus event. At the same time, we began to notice political rumors in Brasilia, of a very similar nature to what happened at the same period in 2019. With the coronavirus issue, what was a previously expected growth of around 2.5% for 2020, is now slightly below 2%. The main consequence of this radical scenario change was the fall of the stock market and also of interest rates. Our portfolio was hardly affected during this entire crisis, and not by coincidence, since we had exactly these two positions in the portfolio, i.e., bought on the stock exchange and receiving interest. Looking ahead, we continue to believe that the political rumors will end soon, and that the reform agenda in Brazil will continue to go ahead, especially from congress' more positive attitude towards understanding the importance of reforms for the country. We believe that Copom should cut interest rates a little more in order to stimulate the economy, which would be in line with what is happening around the world, where other central banks have cut interest rates again. We are maintaining rates and equities positions, with protections on fx.

LatAm

In Mexico, after cutting 25 bps at the last meeting by unanimous decision, putting interest rates at 7%, the idea of a break from Banxico had been growing among market analysts, already in March's meeting. This was reinforced by the sharp drop in the Mexican peso during the coronavirus crisis, since the Mexican central bank has the habit of being concerned about drops in local currency. This thesis falls apart since many central banks around the world are already returning to policies of greater monetary easing. The impact of the coronavirus crisis in Mexico is more on the supply side than on the demand side, due to the shutdown of factories in China and its impact on inputs for the Mexican economy. The cooling of the US economy also increases the chance that Mexico will have another year of economic growth close to zero. Given this situation, we continue with more positive outlooks for the interest rate curve, negatives on the stock market, and now with a more opportunistic trend in the currency.

In Chile, economic data for January looks better than market expectations. This does not change our most negative outlook for the country, given that the problems of the coronavirus crisis will still be present in Chile, and will certainly affect economic activity throughout the year. The upcoming constitutional referendum will also greatly affect the country's short and medium term scenarios. This is because, depending on the type of results there will be, the country may be impacted economically and socially. A referendum with a wide margin of victory for constitutional revision would certainly lead to a very strong expectation of fiscal expansion, with negative impacts on Chilean deficit and debt. While a referendum with a narrow margin of victory could cause street protests to escalate. Despite these more negative outlooks for Chile, we now have a more neutral outlook for the currency and the interest curve.

In Colombia, President Ivan Duque continues to experience declining popularity, now reaching levels close to 24 points. Problems with congress, including the opposition and the very parties that support the president, have ultimately affected how society views the government. The monetary policy report negatively revised the country's potential output, now showing a smaller gap than previously estimated. In theory, this would increase the chances of a tightening of monetary policy; but the coronavirus crisis having direct impacts on Colombia's economic activity—especially since the sharp fall in oil prices—has almost completely ruled out this possibility. The Colombian peso continues to depreciate, but to a lesser extent than other Latin American currencies, given that Colombia still shows ample economic growth in the region, at around 3%. Our outlook for the currency was more negative, while for interest rates it was neutral. But now our outlook is neutral for both the currency and the interest curve.

In Argentina, the debt restructuring process is going through a critical period. Large investors in Argentine securities, as well as the IMF, are negotiating with members of the Ministry of Finance. We remain concerned with the country's state of affairs, in view of the negative real interest rate that is being practiced by BCRA; we therefore do not see how the country can achieve economic stability to then pursue a goal of economic growth that guarantees social stability. The markets continue to have very little liquidity and we see no short-term investment opportunities.

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