BlueLine
ASSET MANAGEMENT

MONTHLY LETTER I May 2020

We are very pleased to announce that our Blue Alpha Fund completed its one-year anniversary at the end of May! We delivered returns above the benchmark and the industry average during this period, strictly following BlueLine's investment philosophy, which undergoes a robust fundamentals analysis, discipline in risk control and construction of portfolios appropriate to the current market regime. This philosophy allowed us to take advantage of opportunities – mainly in rates and equities, both in Brazil and abroad – and to especially preserve investor capital in moments of extreme uncertainty, such as the month of March. We will continue under this work philosophy for the next several years, which has been extensively tested over the last twelve months, pursuing consistent returns and secure resource management.

Results of the month of May. The Blue Alpha fund posted a positive performance of 9 bps in May with 39 bps coming from rates, -34 bps from equities and -2 bps of FX. Cash and costs added +2 bps.

International. The major dilemma abroad right now arises between the speed of reopening economies, especially in the developed block, and the enormous global risks that still exist. In this context, the month of May has become the second month of recovery for the global markets, following the steep drop in March. The long-awaited Covid-19 infection peak in the U.S. and Europe occurred in May and, coupled with the massive amounts of stimuli injected into developed economies, continues to drive markets upwards. In terms of the risks we are monitoring globally, the most pressing is not necessarily in the field of health, but in the geopolitical context, with the escalating tensions between the U.S. and China. Another risk that cannot be completely ruled out is a second wave of infection. So why are the markets still so strong? The answer to that question probably lies in at least two major arguments. The first is that although we have seen an extremely deep and drastic recession, it is probably coming to an end, given that we will be seeing very high economic growth rates in early July, even if starting from a still very depressed base. We all know that markets always "look" at the marginal development of facts, and this applies to all aspects, whether economic, political, or social. The second factor is of an eminently technical nature, which is the fact that risk allocation in general is still very low throughout the world. A major destruction of wealth has been ongoing since March, and with the exception of some classes of investors, the majority still have very low risk allocations. That being said, we believe that the current "Risk On" environment will persist throughout the month of June.

Brazil. May was another very volatile month for Brazilian assets. As if the external uncertainties were not enough, we saw the fall of two ministers from the Bolsonaro government, where the departure of Sergio Moro was most significant for the local markets, especially due to the risk that this event could mean a possible future departure of Paulo Guedes. Brazil is experiencing a time of great economic, political, and institutional fragility, perhaps even greater than that observed in PT governments, given the rapid deterioration of public accounts and the president's untimeliness. The recent roadblock between the president and the STF only underscores the seriousness of the aforementioned point. However, the markets also showed an upswing, especially at the end of the month. This is due to the environment abroad, as well as the fact that some local political agents, such as the House and the Senate, are positioning themselves in favor of creating an institutional truce in the country. The president's approximation to the central parties, despite going against what the president himself affirmed at the beginning of his term, is showing to be something positive in the sense of achieving a minimum degree of political stability. We remain positive in receiving the short curve of short-term interest rates in Brazil, as well as starting a stock exchange portfolio focused on a fundamentalist analysis, especially in sectors that are already heavily discounted. In FX, we are operating in a very opportunistic manner.

LatAm

Mexico, unlike Brazil, is "only" experiencing an economic and public health crisis, and there is no political and institutional crisis underway in that country at this time. Banxico continues to flex its monetary policy in a very cautious manner, while still using extraordinary meetings to speed up the process of monetary easing, always with the fear of damaging the country's financial stability, understood here as being the exchange rate. We remain convinced that terminal interest in Mexico should be less than 4%, which presents significant value in short interest contracts. We also like the currency profile, which has been well-behaved in the last 30 days, especially due to the fact that the technical position of the currency has improved after reaching the record level of 25 pesos per dollar. We also have some exposure to the Mexican stock exchange, as it is one of the most discounted assets in emerging markets.

Chile continues to benefit from China's recovery, especially from the high price of copper. The president's popularity remains high, largely based on the correct measures taken by the local administration in relation to the health problem. The Central Bank of Chile also greatly anticipated its monetary easing cycle, and we therefore no longer see room for additional interest rate cuts in that country. We find the currency profile favorable, even though it is already in a much more appreciated position than the Brazilian real or Mexican peso for example.

In Colombia, the improvement in the oil market undoubtedly provides a relief factor for the Colombian economy, given that 50% of its exports are tied to the commodity. Colombia is the country that suffers the least from the perspective of economic growth in the region, and this has been a positive factor for the local currency. BanRep continues to cut interest rates, now set at 2.75%, and with a high chance that they will continue to fall. In this respect, the interest rate in Colombia is similar to that of Brazil, where BanRep chose to cut 50 bps in contrast to the 75 bps of the last Copom, but increased the frequency of meetings to monthly meetings versus the 45-day Copom term. We continue to enjoy receiving short interest in Colombia and currently have no position in the local currency.

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