BlueLine
ASSET MANAGEMENT

# MONTHLY LETTER I December 2020

**2020 Closing.** Last year was fraught with challenges for resource managers, with the emergence of the global pandemic, the Brazilian political-fiscal crisis, the U.S. elections, and the economic recovery with the arrival of vaccines. But with hard work and dedication, we managed to preserve investor capital at the height of the pandemic, dilute the fiscal risk in Brazil through a more intense use of offshore assets, and take advantage of the U.S. post-election rally through a fairly diversified portfolio, both geographically and by asset class. As a result, we delivered a return of 7.38% (258% of CDI) in the year, with 5.3% volatility. The rates market contributed 562bps to this result, with structural positions in Mexico and more tactical positions in Brazil and the U.S. Despite the major crisis in the second quarter, equities contributed 426bps, a result that was mostly generated abroad. FX results were negative in the first half of the year, but a more aggressive use of this asset class consistent with the global weak dollar trend balanced the accounts in the second half, closing the year at -74bps. In summary, in the tragic year of 2020, we were able to combine agility in preserving capital at dysfunctional moments of the market with the implementation of global and medium-term themes in a diversified portfolio with well-controlled risk.

**Results of the month.** Blue Alpha Fund's performance remained very positive in December (+296bps), supported by the favorable global scenario. The signs of expansion of CBs from developed countries, the passing of the U.S. fiscal package, and early vaccination in a context of robust global economic activity data, continued to generate significant gains in our global equities positions (+217bps) and accelerated gains in our FX positions (+99bps). The risk appetite of global investors coupled with reduced short-term fiscal risks motivated us to return to the local rates market, which along with Mexican rates positions contributed to this book's positive 38bps result. Fund cash and expenses accounted for (-58bps) in December.

**International.** In December, global markets continued the rally that started in November. While November eliminated the U.S. electoral risk, December saw at least two very positive news for the world, namely: (i) the confirmation of the effectiveness of Pfizer's and Moderna's vaccines; and (ii) the passing of the $900-bi COVID fiscal package with massive bipartisan support from the U.S. Congress. Associated with these events, we saw a continued fall in real interest in the U.S., which is largely substantiated by increased inflation break-evens, something that reinforces the thesis of "reflation" in the world. Rising equities and the dollar decline confirmed our medium-term convictions for the global scenario, and therefore we are keeping our global equities positions, from a fairly diversified portfolio, both sectorally and regionally. Similarly, our currency portfolio is being further diversified. The margin is undergoing point adjustments in these two portfolios to increase efficiency in the final allocation of risk. Lastly, we are also maintaining our rates portfolio strategy, i.e., applied in interest in Brazil and Mexico, and taken in interest in the U.S. It is worth mentioning that we are also making marginal adjustments in these rates curves, based on our assessments of the evolution of macroeconomic scenarios in these three countries.

**Brazil.** The scenario we are experiencing is quite favorable for emerging markets, especially for commodity-producing countries with more connections to China. In this context, Brazil stands out primarily in the mining and oil industries. Therefore, we continued to increase our exposure in Brazilian equities in December, something that had started in November. Also, our view is that recent inflationary pressures will lose some momentum and that the second COVID wave could negatively affect the growth scenario in the first quarter of 2021. This is added to Bolsonaro's more cautious approach regarding the non-extension of emergency aid in early 2021. Thus, we do not expect the Central Bank to remove the "Forward Guidance" at first, and therefore we see value in the short part of the DI curve, which still prices 300bps up in 2021. To hedge these two optimistic positions in Brazil, we have some purchase of USD/BRL. We understand that the House election is the great opening event of the new year in Brazil, and therefore we are monitoring it more closely. Regardless of what happens in the House, we feel that the frictions typical of the previous Legislative administration with the Executive is likely to decrease and the Senate will gain importance as mediator of the debates on the country's major issues.

**Mexico.** The Mexican currency has been one of the best-performing assets in the world in recent months. This is directly related to the current level of interest rates in the country, as well as – why not say it – the fiscal prudence adopted by the AMLO administration, even during the hard times of the pandemic. Interest rates in Mexico continue to fall and we think it should continue that way, especially since the recent signs given by the Mexican economy are weaker than expected. The best perspective for the American economy undoubtedly also helps the appreciation of Mexican assets, which clearly does not participate in the commodity cycle boom that we are experiencing, but which stands out for the fiscal situation and the high real interest rates. These are the two positions we like in Mexico and therefore we are keeping them.

**Positioning.** With the continuity of a favorable scenario in the markets, but with price levels in some assets reaching record highs, our strategy is still to recycle the portfolio focusing on assets that benefit from the recovery of global growth, weakening of the dollar, and lower geopolitical noise. This involves further diversifying our equities portfolio, including more countries in the Asia-Pacific region, but also strengthening more cyclical sectors of the U.S. market and global equities in Brazil. In currencies, diversification has also intensified in the short USD strategy, with long positions focused on countries with good growth prospects, with great positive commodity influence, or with good rates carry. Finally, in the interest market, in addition to the more structural position receiving interest in Mexico with protection taken in American treasuries, we are once again placing positions in Brazilian interest rates to take advantage of the favorable global trend, in a context of lower political noise and reduced inflationary risks.

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