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MAKING MONEY WORK FOR YOU.

Inflation and your portfolio

July 26th , 2021

ANALYST INSIGHT

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Inflation and your portfolio

A major topic now on the minds of many investors locally and globally is inflation. This comes as no surprise as we Jamaicans have ourselves already seen some price movements at the pumps as global crude oil prices are currently up 48% year to date. Inflation is simply, the fall in the value of money and a debate into its root cause can swiftly detour into debates revolving around Keynesian economics, demand, and cost push inflation, or if it's simply a result of too much money in circulation. Without speaking too deeply into its origins at the moment, we believe a more practical exercise would be to stay informed as to what are the best ways to protect your personal investment portfolio from the subtle but erosive effects of inflation by looking at past data driven research done on the topic.

Commodities

It is generally thought that in times of inflation it is most reasonable to own real physical assets, whose value tend to rise commensurately with inflation as opposed to financial assets. These assets are typically thought to be commodities (particularly investment commodities such as gold and silver) and real estate. The financial literature tends to be more conclusive as it relates to commodities as opposed to real estate. Mahlstedt and Zagst (2016) in their study on inflation protected investment strategies, noted that adding commodities (i.e. via futures) to a portfolio of stocks and bonds drastically improved performance in inflationary periods particularly in the short run. Interestingly, even though gold is the most popular investment commodity, particularly due to its diversification properties, majority of the literature have found that it is typically the non-investment commodities that performed the best in terms of real returns in high inflationary environments. An explanation for this being the fact that these commodities are typically the ones that are driving a lot of past inflationary cycles that we've seen directly (think crude oil, rare earth metal and copper prices throughout the years).

REITS and Equities

It is also often thought that REITS and equity would offer some amount of protection against inflation. The logic being close to that of commodities, being that they represent some stake in real assets (for the most part) that would therefore increase in value somewhat in-line with the overall price level. While studies have shown this to be true for the most part, it has been seen that this hedge has primarily been over the long run horizon. Narkowitz(2020) noted that while REITS and Equity do have inflation hedging properties they need longer time horizons for which to pass on higher prices and rents to their consumers. It is however noted that while equities performed poorly in the short term due to unexpected inflation, they tend to keep up with prices in the long run.

Bonds

Most research have shown conditional results for the ability of bonds to protect against inflation. That is, they are poor in protecting against inflation in the short term (particularly long maturity bonds) while some have noted that they can present good opportunities depending on the time horizon and the source of inflation. That is high unexpected inflation tends to increase bond yields as investors require higher premiums, which means that inversely bond prices are lower for an overall lower short-term real return. In theory this is due to high inflation eroding the fixed income payments received, leading to a lower present value for bonds. However, some studies have shown that in the case of a short-term unexpected inflationary shock, in the long run, long term bonds have shown the ability to generate excess returns. This is because of the higher yields dominating the price declines in producing higher total returns as inflation subsides.

Practical Portfolio Implications

We wouldn't expect you to start hoarding bananas in your backyard to hedge against inflation, for there are other ways to incorporate commodities in your portfolio. This can be done by gaining exposure to entities that are heavy in specific commodities sectors (think oil stock and bonds in an oil price boom, or the sovereign debt of these commodity exporting countries) or to even incorporate commodity ETFs and futures into your portfolio. It may also be helpful to include gold exposure for the diversification benefits due to its low correlation with other asset classes. As it relates more generally to equity and REITs in your portfolio this decision might depend on your investment horizon and outlook. As we have noted they both tend to hedge well in the long run and hence it would be recommended that if your investment horizon is sufficiently long and/or if you have the belief that the inflationary period might be extended, to increase your exposure to these asset classes. Lastly it might be prudent to cut your exposure to longer term bonds if you wish to reduce your inflation risk, particularly in the short run.

Refereces/further readings
Attié, A. P., & Roache, S. K. (2009). Inflation hedging for long-term investors. *IMF Working Papers*, *2009*(090).
Hoevenaars, R. P., Molenaar, R. D., Schotman, P. C., & Steenkamp, T. B. (2008). Strategic asset allocation with liabilities: Beyond stocks and bonds. *Journal of Economic Dynamics and Control*, *32*(9), 2939-2970.
Mahlstedt, M., & Zagst, R. (2016). Inflation protected investment strategies. *Risks*, *4*(2), 9.

LOCAL EQUITIES MARKET

For the week ended Friday, our local stock market declined week-over-week. The JSE Combined Index decreased by 0.23%, the Main Market Index declined by 0.17%, the JSE All Jamaican Composite Index fell by 0.06%, the JSE Junior Market Index decreased by 0.93%, and the JSE USD Equities Index increased by 1.61%.

During the week, Radio Jamaica Limited was the largest gainer, rising by 27.04% to close at J$2.12. The biggest loser was Elite Diagnostic Ltd which fell by 11.57% to close at J$3.18.

Year to Date, The Junior Market Index (+27.45% YTD) continues to outpace its Main Market counterpart (+6.00% YTD) by a wide margin.

As of Friday July 23, 2021, Overall Market activity resulted from trading in 110 stocks of which 38 advanced, 61 declined and 11 traded firm. Market volume amounted to 115,042,782 units valued at over $635,947,615.98. Stanley Motta Limited Ordinary was the volume leader with 34,718,065 units (30.18%) followed by Radio Jamaica Limited with 14,770,053 units (12.84%) and Sagicor Select Funds Limited - Financial with 11,304,673 units (9.83%).

Revisiting relevant news during the week:

Caribbean Cream Limited, which trades under the name KREMI, is moving forward with its US$2-million liquefied natural gas (LNG)-powered plant, which it initially announced in January this year.
https://www.jamaicaobserver.com/business-report/caribbean-cream-moves-forward-with-us-2-million-lng-plant-installation-and-commissioning-of-plant-expected-by-the-end-of-2021_226830?profile=1056

Low-cost American carrier Frontier Airlines continues its Caribbean expansion with more non-stop flights to Jamaica
https://www.jamaicaobserver.com/business-report/frontier-airlines-expanding-flights-to-jamaica-new-flights-will-begin-this-november_226831?profile=1056

As global markets continue to recover from the novel coronavirus pandemic-induced declines in 2020, QWI Investments Limited's performance continues to improve as its net profit for the quarter ending June 30 improved by 42 per cent to $163.71 million.
https://www.jamaicaobserver.com/business-report/qwi-investments-profits-catapult-on-recovering-markets_226833?profile=1056

Antigua and Barbuda-based cryptocurrency trading platform, FTX trading Limited, has closed a US$900-million fund-raising round, describing it as "historic".
https://www.jamaicaobserver.com/business-report/antiguan-crypto-exchange-closes-us-900-m-fund-raise_226773?profile=1056

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Index	23/07/2021	16/07/2021	31/12/2020	Week/Week	Year-to-Date
JSE Main Market	419,356.37	420,071.66	395,614.93	-0.17%	6.00%
JSE Junior Market	3,369.03	3,400.73	2,643.38	-0.93%	27.45%
JSE Combined Market	422,064.63	423,042.60	392,435.92	-0.23%	7.55%
JSE USD Equities Market	188.95	185.95	186.30	1.61%	1.42%
JSE All Jamaican Composite Index	458,112.26	464,466.25	433,521.09	-1.37%	5.67%

INTERNATIONAL DEVELOPMENTS

Stocks ended the week higher, rebounding from a sell-off on Monday. The advance was somewhat narrow, however, with much of the gains concentrated in technology and internet-related giants—the so-called FANG+ stocks. Relatedly, growth shares handily outperformed value stocks for the fifth consecutive week, leaving them ahead for the year to date, according to Russell benchmarks. Trading volumes were also especially light, with the number of shares trading hands on Thursday at their second-lowest level of the year. Early Monday, the Russell 2000 Index was down 10% from its closing high on March 15, marking its first correction in more than one year.

Many observers attributed the steep declines at the start of the week to growing fears about the spread of the delta variant of the coronavirus. Cases and hospitalizations rose in many parts of the country, particularly in states with low vaccination levels. Stocks tied to the reopening of the economy, such as cruise operators and airlines, fared particularly poorly. Energy stocks were also especially weak, as oil prices suffered their biggest daily decline since April 2020 after OPEC and other major oil exporters struck a deal to increase output.
https://www.troweprice.com/personal-investing/resources/insights/global-markets-weekly-update.html#US

Investment-grade corporate bond spreads—the extra yield offered over Treasuries and an inverse measure of the sector's relative appeal—moved wider early in the week on light flows, as concerns regarding the delta variant and inflation weakened sentiment. However, spreads retraced throughout the week, aided by the rebound in equities and a steepening Treasury yield curve.
https://www.troweprice.com/personal-investing/resources/insights/global-markets-weekly-update.html#US

Top 5 Things to Watch in Markets in the Week Ahead

1. **Fed taper talk** - The Fed wraps up its two-day meeting on Wednesday and its statement will be scrutinized for any mention of the timeframe for tapering its asset purchase program, although Chairman Jerome Powell made it clear in his recent testimony to Congress that the U.S. economy still needs the central bank's full support.

2. **Data dump** - Aside from the Fed meeting, investors will get an update on the strength of the U.S. economy with an end-of-month data dump.

3. **Earnings deluge** - U.S. earnings are kicking into high gear and investors will be watching the largest tech names to gauge whether a recent shift away from reflation trade and into growth stocks that led markets for the last decade will continue.

4. **Market volatility** - Growth and value stocks seesawed for much of last week as investors weighed the surging Delta variant against upbeat earnings results and economic data. "There's push and pull, there's clearly conflict in the market," Chris Zaccarelli, chief investment officer at Independent Advisor Alliance in Charlotte, North Carolina told Reuters. "There's a strong difference of opinion as to whether the future's bright or whether there are clouds on the horizon."

5. **Euro area recovery** - In the euro zone, second quarter GDP data on Friday will give investors some insight in the strength of the bloc's economic recovery from a double dip recession as vaccinations pick up.

https://www.investing.com/news/economy/top-5-things-to-watch-in-markets-in-the-week-ahead-2567327

Index	23/07/2021	16/07/2021	31/12/2020	Week/Week	Year-to-Date
Dow Jones	35,061.55	34,687.85	30,606.48	1.08%	14.56%
S&P 500	4,411.79	4,327.16	3,756.07	1.96%	17.46%
NASDAQ 100	14,836.99	14,681.38	12,888.28	1.06%	15.12%
FTSE 100	7,027.58	7,008.09	6,460.52	0.28%	8.78%
Euro Stoxx 50	4,109.10	4,035.77	3,552.64	1.82%	15.66%

Local Economic Conditions

Local Foreign Exchange Market

- Our local currency depreciated by 0.22% against the U.S. Dollar week on week to settle at $155.34 as at close of trade Friday, relative to $153.89 per US$1.00 at the end of the prior week. Year to date, the Jamaican dollar has depreciated by approximately 8.90%.

Interest Rates and Inflation

- The BOJ continues to maintain an accommodative monetary policy since gaining its independence to support the current environment. As at their latest policy decision announcement, they maintained rates a 0.50%.

- At this rate, based on its assessment, the BOJ notes that inflation will generally continue to remain within the target of 4.0% to 6.0% over the next two years. This is despite recent inflation overshoots Internationally.

- As at June 2021, point-to-point was recorded at 4.3%.

Currency Pair	23/07/2021	16/07/2021	31/12/2020	Week/Week	Year-to-Date
JMD: USD	155.34	155.00	142.65	-0.22%	-8.90%
JMD:CAD	127.14	124.49	111.41	-2.13%	-14.12%
JMD:GBP	213.89	214.32	193.66	0.20%	-10.45%

Unit Trust Performance

- Year to Date, The Money Market Fund has increased by 2.26%, the FX Bond Portfolio has increased by 0.69%, the F.X. Growth Portfolio increased by 3.75%, the Real Estate Portfolio has decreased by 4.01% and the Capital Growth Fund has grown by 8.33%.

- Barita's Collective Investment Schemes ("CIS") offer the opportunity for investors to remain invested in the market at this delicate stage of the market cycle; moreover, there is a diversification benefit and opportunity to have a professional portfolio manager make the best-in-class professional judgements on your behalf.

- The F.X. Growth Fund, which is benchmarked against the S&P 500, has increased by 3.75% year to date.

- As at July 14th, 2021, the Capital Growth Fund has delivered a YTD return of 8.33%, which surpasses its benchmark of the JSE Combined Index which has grown by 7.55% over the same period.

- The FX Bond Portfolio remains an attractive fixed-income portfolio, particularly when viewed within the context of global interest rates which have declined significantly as central banks maintain low policy rates to drive the economic recovery.

"A market downturn doesn't bother us. It is an opportunity to increase our ownership of great companies with great management at good prices."

– Warren Buffett

Unit Trust

Unit Trust Fund	29/04/2021	14/07/2021	Week/Week Return	Year-to-Date Return	1 Year Return	Yield
Capital Growth	91.94	92.18	-0.26%	8.33%	19.69%	-
Money Market	15.1092	15.1048	0.03%	2.26%	3.42%	1.59%
Income Portfolio	100.00	100.00	-	-	-	2.25%
FX Bond Portfolio (US$)	1.3656	1.3676	-0.15%	0.69%	5.20%	2.04%
Real Estate Portfolio	5,601.32	5,626.00	-0.44%	-4.01%	-10.45%	-
FX Growth Portfolio	1.0360	1.0397	-0.36%	3.75%	12.50%	-

The investor's chief problem—and his worst enemy—is likely to be himself. In the end, how your investments behave is much less important than how you behave.

- Benjamin Graham

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Equities

Stock Ticket	Stock Information (As at July 23th, 2021)	Analyst Outlook
WISYNCO Wisynco Group Ltd	P/E: 21.75 P/B: 3.94x Price: J$15.66 Div Yield: 1.21%	**OVERWEIGHT** The local fiscal support to both households and businesses was instrumental in maintaining individuals' consumption capacity, particularly those furloughed and made redundant, which supported the demand for consumer staples distributed by manufacturers and distributors Wisynco. We expect that with continued fiscal support through either direct household support or government spend on projects to stimulate employment, Wisynco's business will thrive in this environment.
LASM Lasco Manufacturing	P/E: 15.71x P/B: 2.75x Price: J$5.25 Div Yield: 1.16%	**MARKETWEIGHT** Our expectation is for the Company to continue on its growth trajectory, supported by the improving economic backdrop of the global economy, which may manifest in increased domestic demand for goods and services. With increased stopover arrivals and planned reopening of key industries such as entertainment and education (face-to-face teaching), there are sufficient catalysts to spur further growth in 2021. However, this isn't without challenges as the global supply bottleneck will manifest itself in LASD's margins, requiring management to remain prudent in their working capital management such that higher imported inflationary pressures are not corrosive to the bottom line. Our MARKETWEIGHT recommendation balances our outlook on the company against the potential upside embedded in our estimate of fair value (as per Barita's July 15, 2021 equity report) for the company.
LASD Lasco Distributors	P/E: 14.90x P/B: 2.03x Price: J$3.86 Div Yield: 1.32%	**OVERWEIGHT** Our expectation is for the Company to continue on its growth trajectory, supported by the improving economic backdrop of the global economy, which may manifest in increased domestic demand for goods and services. With increased stopover arrivals and planned reopening of key industries such as entertainment and education (face-to-face teaching), there are sufficient catalysts to spur further growth in 2021. However, this isn't without challenges as the global supply bottleneck will manifest itself in LASD's margins, requiring management to remain prudent in their working capital management such that higher imported inflationary pressures are not corrosive to the bottom line.

Ratings Definitions

OVERWEIGHT/BUY
Exposure to this asset should be between 5% and 10% of your total portfolio

UNDERWEIGHT
Reduce exposure in your portfolio to less than 5% for this particular asset

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Equities

Stock Ticker	Stock Information (As at July 23th, 2021)	Analyst Outlook
SGJ Scotia Group Jamaica Limited	P/E: 12.65x P/B: 1.02x Price: J$38.83 Div Yield: 3.61%	**MARKETWEIGHT** SGJ's growth has slowed, even prior to the pandemic. Consequently, within the context of the pandemic, the Group reported a considerable net profit decline of 31.4% in FY2020. Notwithstanding, the most recent performance demonstrates that coming out of the pandemic, the Group will report relative growth in FY2021, predominantly reflecting lower ECL, FX gains given SGJ's position in the FX market, and gains from the extinguishment of debt. Beyond FY2021, however, we expect a slowdown in growth, as ECL reduction is tempered relative to FY2021 and as the Group no longer benefits from a gain on extinguishment of debt. Importantly, we also consider the Group's strong liquidity, capital adequacy, and consistent dividend payout which is at an attractive yield of 3.58%. Given its strong balance sheet and consistently above-average dividend yield, we believe SGJ is a good dividend income stock.
VMIL Victoria Mutual Investments Limited	P/E: 21.30x P/B: 2.32x Price: $6.35 Div Yield: 0.16%	**MARKETWEIGHT** On balance, we believe the upside seen by VMIL in Q1 2021 potentially represents the most Year-over-Year (YoY) upside the company will realize in FY2021 and should be the main driver of improved YoY profitability for the 2021 financial year. However, we believe the market dynamics will weigh on YoY performance, unless there's a significant improvement in business origination, beyond prior years, on the back of a strengthening economy or increased capital that can then be deployed towards growth initiatives. With that said, our MARKETWEIGHT recommendation balances the risks that remain against the potential upside embedded in our estimate of fair value (as per Barita's July 16, 2021 equity report) for the company.

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SEP Seprod Limited	P/E: 17.23x P/B: 2.93x Price: J$67.52 Div Yield: 0.89%	**OVERWEIGHT** Seprod has undergone significant structural changes within the last 5-years aimed at improving the underlying performance of the company. Within this period, particular emphasis has been placed on optimizing the distribution, warehousing and logistics capabilities of the company. This gradual, multi-year, improvement was accomplished through reinvestment within the organization coupled with strategic acquisitions aimed at increasing the distribution reach and quality of the company. Another major change was the closure of the Group's loss-making sugar division; a move that enhanced shareholder value. These changes have positioned Seprod to deliver robust growth through an expansive product mix and access to consumer markets both locally and regionally.
PROVENJMD Proven Investments Limited	P/E: 12.89x P/B: 0.86x Price: $34.99 Div Yield: 2.25%	**OVERWEIGHT** Given the current economic environment, characterized by low interest rates and increased uncertainty, PIL has shifted from the carry trade business to more private equity and real estate ventures, thereby allowing for diversification benefits to be realized - particularly as it relates to the "spreading" of risk. Given the business model of PIL wherein capital is used to acquire strategic assets, this APO is expected and should make the stock accessible to a wider pool of investors. At present, only a small subset of listed companies pursue private equity investments which makes PIL an attractive security for investors who want the liquidity the stock market provides as well as exposure to non-listed companies that can provide value.

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PROVENUS Proven Investments Limited	P/E: 12.73x P/B: 0.85x Price: US$0.24 Div Yield: 3.25%	**OVERWEIGHT** Given the current economic environment, characterized by low interest rates and increased uncertainty, PIL has shifted from the carry trade business to more private equity and real estate ventures, thereby allowing for diversification benefits to be realized - particularly as it relates to the "spreading" of risk. Given the business model of PIL wherein capital is used to acquire strategic assets, this APO is expected and should make the stock accessible to a wider pool of investors. At present, only a small subset of listed companies pursue private equity investments which makes PIL an attractive security for investors who want the liquidity the stock market provides as well as exposure to non-listed companies that can provide value.
SCIJMD Sygnus Credit Investments	P/E: 13.21x P/B: 0.63x Price: J$14.96 Div Yield: 2.40%	**OVERWEIGHT** Sygnus provides funding to Mid-Size firms within the lending market, which is considered to have a higher risk and generally overlooked by providers of traditional financing forms. This provides a largely untapped/under-tapped niche market within the Caribbean lending space for Sygnus, a few direct competitors. The flexibility in the financing terms offered by the Company is a clear advantage to borrowers, and it allows SCI to manage its credit risk to generate double-digit risk-adjusted returns on investments, which, consequently, bolsters shareholder value.
SCIUSD Sygnus Credit Investments	P/E: 21.05x P/B: 1.02x Price: US$0.16 Div Yield: 1.56%	**OVERWEIGHT** Sygnus provides funding to Mid-Size firms within the lending market, which is considered to have a higher risk and generally overlooked by providers of traditional financing forms. This provides a largely untapped/under-tapped niche market within the Caribbean lending space for Sygnus, a few direct competitors. The flexibility in the financing terms offered by the Company is a clear advantage to borrowers, and it allows SCI to manage its credit risk to generate double-digit risk-adjusted returns on investments, which, consequently, bolsters shareholder value.

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CCC Caribbean Cement Company	P/E: 24.61x P/B: 6.03x Price: J$92.54 Div Yield: 0.00%	**OVERWEIGHT** Throughout the COVID-19 pandemic, all industries have been affected by what has been a significant downturn in aggregate demand as the pandemic has created a need for persons to reduce travelling and physical interaction. Despite this setback which predominantly materialized in Q2 of 2020, the construction industry has rebounded significantly (7.0% in Q3 2020 and 6.2% in Q4 2020), ahead of many other industries and well ahead of the overall economy. This strong growth over the last two reported quarters has been a significant tailwind for Caribbean Cement and the company has consequently seen a significant increase in the demand for its product, well in excess of previous years. On the heels of what has been a great year for the company, management expects demand to increase further, fueled by upcoming government projects that will require substantial cement deposits. The recent government budget lends to this expectation as one of the main components of the government's SERVE Programme is infrastructure development. With that said, the company is positioning itself to meet this demand while maintaining its more efficient cost structure which was displayed in 2020, chief among these was the reduction of debt, which in turn reduced the company's cost of debt.
LAB The Limners and Bards Limited	P/E: 19.29x P/B: 5.75x Price: J$ 3.09 Div Yield: 2.40%	**OVERWEIGHT** The LAB provides a unique opportunity for investors to get exposure to the first and only advertising and film production company listed on the Jamaica Stock Exchange (JSE). The Lab's business model is built on providing innovative solutions to clients through its main services including its brand/communication strategy, campaign concepts & execution, media buying, and film production. Throughout the pandemic, the company has repositioned its business to meet the demand of clients who needed digital solutions. Consequently, while many industries and companies faltered in 2020, The Lab reported strong top and bottom-line growth of 44.30% and 34.13%, respectively. This growth has continued into 2021, reflecting significant double-digit growth in two of the company's three operating segments. Against the backdrop of a strong, stable business model coupled with robust financial performance, we have issued an OVERWEIGHT recommendation for The Limners and Bards Limited.

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CPFV Eppley Caribbean Property Fund SCC	P/AFFO: 35.28x Price: J$42.22 AFFO Yield: 2.95%	**OVERWEIGHT** Since Eppley became the investment manager of the fund, there has been a material improvement both in portfolio's country exposure and type of real estate structures. This has led to a steady increase in the total square feet of the portfolio and increase Net Asset Value (NAV) with diversification. The Fund's pivot towards introducing Jamaican assets, especially in the industrial space will have a positive material impact on the company's long-term performance. This as the Manufacturing and Distribution (M&D) and construction industry have shown material resilience to the impact of COVID-19. As such, the continued focus on improving value to shareholders through divesting away from Barbados and retail properties will act as a positive tailwind for the long-term performance of CPFV.
MAILPAC Mailpac Group Limited	P/E: 21.21x P/B: 5.27x Price: J$ 3.82 Div Yield: 3.93%	**OVERWEIGHT** Having raised just under $500 million in its November 2019 junior market initial public offering (IPO), by March of 2020 the global economy was grappling with the COVID-19 crisis. This posed both a challenge and an opportunity for the Mailpac Group given the sudden and immediate need for e-commerce capabilities in light of social distancing and other non-medical interventions to reduce the spread of the virus. That the company was able to generate $1.7 billion in revenue during 2020 is demonstrative of the management's agility and competence of the company's leadership. They were able to pivot in building both scale and capacity, which are likely to sustain Mailpac's performance prospectively, given the likely scenario that e-commerce is likely to become more ensconced among Jamaica consumers, across various social classes.

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