Threats To Global Growth & How Investors Should Position

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ANALYST INSIGHT

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Threats To Global Growth & How Investors Should Position

At the start of 2020, the world as we knew it, pivoted into an unknown, with ever-changing variables. Over time, these variables have shifted how investors maneuver the markets, their understanding of the role of fundamentals in the valuing of securities, as well as the need to explore investments outside the realms of traditional investing. As investors search for opportunities to maximize returns within the new norms, there exists several underlying risks to global macroeconomic stability that inherently hinder growth acceleration within the global economy. The nature of these risks includes geopolitical risk, inflationary risk, interest rate risk, and supply chain risk, to name the most prominent ones faced at the moment. All these risk factors compound to create an environment that has the potential to drive significant downside for investors who are not able to carefully mitigate these risks. In this article, we delve into the most topical issues that fall within these stated risk buckets.

Geopolitical Risks

The situation developing in Eastern Europe between Russia and Ukraine seems to be escalating quickly, with Russian troops at the Ukraine border now reaching 130,000. The US has stated that they have strong intelligence indicating that they expect a Russian attack on Ukraine before the end of the winter Olympics; which is slated to end February 20,2022. This poses a significant threat to the global economy and capital markets, as the uncertainty surrounding stability in Europe negatively affects capital market developments and ultimately affects the deployment of capital by investors. Russia is the third-largest oil producer globally and if the country is actively engaged in combat, this may reduce its ability to maintain oil production which may result in the global supply of oil being lowered. This scenario would result in higher oil prices which may lead to further inflationary pressures as oil is a major commodity used in many facets of life. A reduction in output by Russia could lead to increased fuel prices in Jamaica. Petrojam currently uses the US Gulf Coast as a reference point. Lower overall global output could result in the Jamaican consumer experiencing even higher fuel costs. With oil and gas being a major constituent of many production processes this could result in increased costs being associated to other products as manufacturers may not be able to absorb all these costs.

Supply Chain Risks

With the onset of the pandemic, the world has been suffering from supply chain disruptions and dislocation which have been crippling several retail and manufacturing companies. This has been brought about as a result of shorter working hours due to lockdown restrictions, lower productivity due to sickouts from the virus, and the shortage of raw materials that are needed for several manufacturing processes. The disruptions in the global supply chain network has resulted in the Jamaican consumer having to spend more for goods and products, as companies pass increased costs onto customers. In many cases, while costs have been passed onto consumers, some costs have been absorbed by companies, resulting in lower margins as compared to the pre-pandemic era. Richard Pandohie, CEO of Seprod, and former President of the JMEA, has stated that the new operating paradigm that we operate in now consists of delayed lead times, increased shipping costs and increased fuel prices. All these realities have resulted in companies reporting lower gross margins. The reduction in gross margins has the ability to erode shareholders' value as this ultimately results in reduced profitability; thus lower returns for shareholders.

Inflation and Interest Rate Risk

As commodity prices and production costs increase, manufacturers and retailers have had to pass on these costs to their customers which, when coupled with supply chain issues, has been a major driver of heightened inflation. To combat these inflationary pressures, central banks have taken a hawkish stance; marked by raising rates and reducing liquidity to combat the rising inflation. These rate increases may result in the cost of capital via debt and even equity, increasing, and as such may hamper the growth and expansionary prospects of companies as well as increase their interest expense, as the cost of loans or credit facilities become greater and as such, presents the potential for earnings erosion. Taken together, these can ultimately reduce companies' profitability and ultimately decrease shareholder value.

Conclusion

As investors navigate the new paradigm, it's prudent to analyze the degree of exposure that their underlying assets have to these risk buckets and as such, limit this exposure across the various risk areas identified. When selecting investment opportunities, investors should target companies based on their exposure to geopolitical influences and ability to sufficiently navigate these. More specific to the current challenges, focus must be given to those companies' ability to mitigate supply chain disruptions, how leveraged the companies are and how significantly interest rate increases would affect their earnings. Typically, companies best positioned to mitigate increasingly challenging times such as these, are those with strong balance sheets that are also well positioned in their respective industries.

Investment Playbook

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Equities

Stock Ticket	Stock Information (As at February 11, 2022)	Analyst Outlook
WISYNCO Wisynco Group Limited	P/E: 20.14x P/B: 4.30x Price: $19.74 Div Yield: 1.52%	**OVERWEIGHT** Throughout the pandemic, Wisynco has managed to improve its operational efficiency but given the effects of COVID-19 on industries such as tourism and education, the Company was unable to deliver significant revenue growth. Now, with tourism rebounding and schools operating at a greater level, Wisynco has married its improved operational efficiency with stronger revenue growth, allowing for significant net profit growth. As tourism is expected to continue growing towards its pre-pandemic level of output, we expect Wisynco to continue to perform well.
JMMBGL JMMB Group Limited	P/E: 6.88x P/B: 1.25x Price: $41.99 Div Yield: 2.02%	**OVERWEIGHT** Given its relatively low P/E ratio and considering the Group's consistently strong performance throughout the pandemic, the market has been underpricing JMMBGL significantly, relative to its local counterparts. In recognition of this, the JMMBGL Directors approved a share buyback program which should begin in FY2022/23 which begins on April 1, 2022. Share buyback programs reduce the number of shares outstanding. As the supply of shares in the market reduces from the share buyback, share price increase is likely to follow as demand for the stock outweighs supply.
LAB The Limners and Bards Limited	P/E: 23.65x P/B: 7.13x Price: J$ 3.89 Div Yield: 2.83%	**OVERWEIGHT** The LAB is the only listed Creative Agency on the JSE. Throughout the pandemic, the demand for the services provided by the Company has been strong. In FY2021 alone, revenue grew by 35%, an indication of the demand for the Company's services while net profit grew by 22%. With consistently positive cash flows and a cash balance that is 1.4x larger than all the Company's liabilities, we believe the Lab is poised to invest its capital efficiently towards further growth. The first step towards this is the phased roll-out of its brainchild, "SCOPE Caribbean".

Ratings Definitions

OVERWEIGHT/BUY

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

MARKETWEIGHT/HOLD

Exposure to the asset should be equal to 5% of your total portfolio

UNDERWEIGHT

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

SELL

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LASD Lasco Distributors	P/E: 14.08x P/B: 1.83x Price: J$ 3.79 Div Yield: 1.72%	**OVERWEIGHT** Our expectation is for the Company to continue on its growth trajectory, supported by the improving economic backdrop of the global economy, which should manifest through continued domestic demand for goods and services. With increased stopover arrivals and the reopening of key industries such as entertainment and education (face-to-face teaching), there are sufficient catalysts to spur further growth in 2022. However, this isn't without challenges as the global supply bottleneck has affected LASD's margins. In response, management has prudently managed operational costs such that higher imported inflationary has not completely eroded the bottom line, resulting in continued growth..
SCIJMD/ SCIUSD Sygnus Credit Investments	P/E: 9.00x / 11.42x P/B: 0.62x / 0.79x Price: J$15.16 / US$0.13 Div Yield: 2.37% / 1.93%	**OVERWEIGHT** Sygnus' business model is built on providing capital and direction to the underbanked, targeting the middle market. To accomplish this, the Company has executed several equity raises, the most recent of which was its APO launch in December 2020. Given the increase in its weighted average number of shares, EPS growth has not mirrored the double digit growth in net profit attributable to shareholders. However, we must indicate that continued growth at this level will drive higher EPS growth, once further dilution does not occur. Moreover, the stock trades at significant discount relative to peers both from a P/E perspective and a P/B perspective. At present, the market is pricing Sygnus at a seep discount to its book value per share which we believe is very wrong.
PROVENJMD/ PROVENUSD Proven Investments Limited	P/E: 12.27x / 11.10x P/B: 1.02x / 0.92x Price: J$33.69 / US$0.21 Div Yield: 3.47% / 3.69%	**OVERWEIGHT** Proven has shown strong revenue and profit growth throughout the current financial year, a performance driven by the Group's accretive acquisitions. Most notable among these include JMMBGL and Roberts Manufacturing Company Limited. The company continues to demonstrate its appetite for growth through acquisitions as evidenced by the recent 100% acquisition of Fidelity Bank (Cayman). Given the company's history of acquiring companies with accretive value, we expect Fidelity will be similar. Coupled with this, we believe Proven is trading at favourable PE and PB multiples relative to the market

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GENAC General Accident Insurance Company Ltd.	P/E: 13.84x P/B: 2.29x Price: J$ 6.78 Div Yield: 3.24%	**OVERWEIGHT** With inflation on the rise, domestic interest rates are being increased by the Bank of Jamaica. This should support improved investment income for GENAC as the environment is better suited to generate greater returns on its insurance float. Further, the Company has demonstrated greater operational efficiency throughout FY2021 which we expect to continue as GENAC properly streamlines its new operations in Trinidad and Barbados. We also note that GENAC should continue to benefit from its relationship with the large Musson Group which would allow the to form imperative strategic relationships with other Musson group entities and customers.
VMIL Victoria Mutual Investments Limited	P/E: 15.48x P/B: 2.34x Price: $7.12 Div Yield: 2.18%	**OVERWEIGHT** Victoria Mutual has recently rebranded under the "VM Group". By association, there has been implications for VMIL. For example, the Company has been significantly more active in the capital markets through its investment banking arm. We expect continued growth in the investment banking space will add considerable value to the Company's bottom line which has already shown clear improvement throughout FY2021.

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MAILPAC Mailpac Group Limited	P/E: 19.56x P/B: 13.44x Price: J$ 3.13 Div Yield: 3.51%	**MARKETWEIGHT** During the peak periods of the pandemic, MAILPAC benefited immensely as online shopping became a larger share of shoppers' wallets. In large part, this period of heavy COVID-19 fear has reduced and while we anticipate online shopping will remain integral for the everyday consumer, the outsized growth we witnessed in FY2020 will likely soften further. Admittedly, the Company has a fairly robust balance sheet with more cash than total liabilities which we believe places MAILPAC in a position to make growth-inducing investments. The current slowdown in demand and consequently revenue and profit growth, matched with the Company's fairly strong balance sheet underscore our MARKETWEIHT recommendation
SEP Seprod Limited	P/E: 16.21x P/B: 2.54x Price: J$ 62.07 Div Yield: 2.09%	**MARKETWEIGHT** Seprod has been considerably affected by global supply chain issues that have increased the Company's cost of sales. While this has occurred, instead of raising prices to consumers equivalently, Seprod has absorbed some of these costs which has affected profitability. To help mitigate this, the Group has improved its operational cost management which has had positive implications on the Group's Q3 2021 performance. Notwithstanding, the cost of sales remains elevated, and has only trended upwards throughout FY2021, with no clear methods to manage or reduce the current pace of the increase. Therefore, while we expect current operational cost controls to help, the uncertainty regarding cost of goods remains an ever-present threat to Group profit growth.

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SGJ Scotia Group Jamaica Limited	P/E: 13.61x P/B: 1.01x Price: J$ 36.74 Div Yield: 4.22%	**UNDERWEIGHT** The greatest driver of profitability in FY2021 was the reduction of Expected Credit Losses (ECL) relative to the previous year as the economic backdrop improved. Scotia is not likely to have this benefit recur, at least to the magnitude it did in FY2021. This, coupled with no clear path to growing its main revenue lines such as net interest income as well as fees and commission income, particularly in an industry that is highly competitive suggests to us that SGJ is unlikely to realize any significant growth in its bottom line, and consequently, is unlikely to deliver significant share price growth for investors. While this is the case, we much, however, note that SGJ is a consistent source of relatively attractive dividends which makes the Company a good asset for some investors with a clear preference for income.

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Monitoring List

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Equities

Stock Ticker	Stock Information (As at February 11, 2022)	Comments
ECL Express Catering Limited	P/E: 18.26x P/B: 22.02x Price: J$ 5.66 Div Yield: N/A	Given ECL's significant exposure to tourism, the ongoing rebound in the industry bodes well for the Company's FY2022 performance, relative to its FY2021 performance
LUMBER Lumber Depot Limited	P/E: 14.33x P/B: 6.80x Price: J$3.87 Div Yield: 1.55%	LUMBER represents an option to gain exposure to the construction sector which has been a relatively resilient and fast-growing sector. With this sector tailwind, Lumber has shown strong revenue growth since its 2019 listing and the current Trailing Twelve Months (TTM) profits is 39.5% higher than financial year 2021 earnings. There were, however, hiccups in the last quarterly earnings which was impacted by lock down measures, but we are still monitoring how the company progresses given the loosening of restrictions. We also note that despite the growth it has shown over the last 2 years, the stock still trades an attractive PE compared to junior market peers.
TROPICAL Tropical Battery Company LTD	P/E: 16.59x P/B: 2.15x Price: J$1.46 Div Yield: 0.68%	Tropical Battery has been aggressively pursuing revenue diversification strategies, to not be entirely dependent on auto battery and auto accessory sales. This is evident by the company's recent launch of three new subsidiaries aimed at providing renewable energy solutions for commercial customers. The company has recently implemented a new inventory management system that has yielded improved operational efficiencies. We believe that this company will continue to grow as they build out new revenue lines, as they improve operational efficiencies and hence are worth monitoring.
MDS Medical Disposables and Supplies	P/E: 14.49x P/B: 1.79x Price: J$7.10 Div Yield: 0.99%	Medical Disposables and Supplies have quietly been diversifying its revenue streams over the last 2 years. This is inclusive of its purchase of Cornwall Medical and Dental Supplies Limited (CMDL) which has since been consolidated into the company's financial as of their second quarter 2021. This increases the company's exposure to the dental supplies space and also expands their reach into the eastern end of the island. The company has also shifted to providing more confectionary products and we believe its expansion and diversification efforts are worth watching.

The "Monitoring List" represents stocks that are on our radar as our initial expectation for these companies is positive. However, no official recommendation is presented as these stocks are still being evaluated.

Unit Trust

Unit Trust Fund	09/02/2022	02/02/2022	Week/Week Return	Year-to-Date Return	1 Year Return	Yield
Capital Growth	94.22	92.8613	1.46%	2.46%	10.09%	-
Money Market	15.2747	15.218	0.37%	0.33%	2.69%	0.87%
Income Portfolio	100.00	100	-	-	-	3.13%
FX Bond Portfolio (US$)	1.3745	1.3756	-0.08%	-0.27%	1.57%	2.86%
Real Estate Portfolio	5,414.92	5225.9678	3.62%	2.15%	0.27%	-
FX Growth Portfolio	1.0435	1.0469	-0.32%	-3.57%	1.99%	-

"Though tempting, trying to time the market is a loser's game. $10,000 continuously invested in the market over the past 20 years grew to more than $48,000. If you missed just the best 30 days, your investment was reduced to $9,900."

Christopher Davis

LOCAL EQUITY MARKET

For the week ended Friday, the local stock market increased week-over-week. The JSE Combined Index increased by 0.84%, the Main Market Index increased by 0.84%, the JSE Junior Market Index grew by 0.74%, and the JSE USD Equities Index declined by 0.39%. During the week 138 Student Living was the largest gainer, rising by approximately 70.63% to close at J$7.32. The biggest decliner was Fontana Limited which fell by 15.78% to close at J$10.14.

Year to Date, with the ongoing rebound in the local economy, small-cap stocks, reflecting those listed on the Junior Market Index have continued the strong performance seen in 2021, growing by +17.13% YTD, outpacing its Main Market counterpart (1.01% YTD) by a wide margin.

For the week ended Friday February 11, 2022, Overall Market activity resulted from trading in 116 stocks of which 65 advanced, 42 declined and 9 traded firm. Market volume amounted to 164,371,122 units valued at over $1,280,670,068.26. Wigton Windfarm Limited Ordinary Shares was the volume leader with 27,986,854 units (17.03%) followed by Qwi Investments Limited with 18,786,088 units (11.43%) and Future Energy Source Company Ltd Ordinary Shares with 18,256,568 units (11.11%)

Revisiting relevant news during the week:

The Wisynco Group has touted its decision to setup a two-megawatt (MW) liquified natural gas (LNG) power generating plant as the reason it has been able to limit price increases on its products as other manufacturers raise prices from rising fuel costs. The manufacturing and distribution company, which opened the plant in July 2020, has seen its utility costs drop by 45 per cent from $622.30 million in June 2020 to $342.55 million in June 2021.
Price increases tempered

First Rock Private Equity is about to acquire a controlling stake in a petroleum company in Trinidad. The cost to acquire the firm was not disclosed, but First Rock Private Equity is set to take an 85 per cent stake in the entity from the current majority shareholder.
First Rock strikes oil

Gracekennedy is set to launch a new subsidiary, GK Mutual Funds, in the second quarter of this year after receiving approval from the Financial Services Commission (FSC) to enter that market. The conglomerate, which will celebrate 100 years on Monday, said the FSC gave it approval to enter the Collective Investment Schemes (CIS) market.
GK to launch mutual fund

Mailpac Group is keen on exploring opportunities created by the boom in e-commerce across the Caribbean. While there were no significant changes in the company's revenue for 2021, Executive Chairman Khary Robinson shared that "Mailpac is more focused and better equipped to meet its long-term goal of becoming a regional leader in e-commerce fulfilment."
Mailpac repositioning for e-commerce growth

The Seprod Group has released financials showing that last October's fire at its Facey Commodity subsidiary, Facey, has razed its bottom line, sending profits tumbling 25 per cent to $2.16 billion. The fire wiped out over 86 per cent of the finished goods inventory, which also included the Christmas stocks.
Fire burns Seprod's bottom line

Lasco Financial Limited (LasFin), which is seeking to increase its participation in the cambio and remittance industries, indicates that it is willing to onboard agents from the Alliance Financial Limited (AFL network), following the suspension of these operations when AFL was suspended from operating these businesses in December 2021.
Lasco Financial goes after bigger share of remittance pie

Index	11/02/2022	04/02/2022	31/12/2021	Week/Week	Year-to-Date
JSE Main Market	400,154.97	396,802.02	396,155.61	0.84%	1.010%
JSE Junior Market	4,015.44	3,985.87	3,428.30	0.74%	17.13%
JSE Combined Market	410,292.37	406,890.41	401,130.23	0.84%	2.28%
JSE USD Equities Market	203.99	204.79	195.51	-0.39%	4.34%
JSE Financial Index	96.28	96.47	98.05	-0.20%	-1.81%
JSE Man&Dis Index	111.58	108.09	100.38	3.23%	11.16%

INTERNATIONAL DEVELOPMENTS

US

After another volatile week, the large-cap indexes ended the week lower, while the S&P MidCap 400 and small-cap Russell 2000 indexes recorded modest gains. The technology-heavy Nasdaq Composite fared worst and ended roughly 15% from its recent peak, T. Rowe Price traders noted that the tug of war between healthy earnings growth and fears over monetary tightening dominate sentiment. Warnings from U.S. officials that a Russian invasion of Ukraine might be imminent may have also contributed to a late-week sell-off. Declines in mega-cap technology stocks—weighed on the broader indexes on Monday, but the so-called reopening trade helped stocks regain their footing at midweek. Shares in restaurants, hotels, casinos, air and cruise lines, and online travel agency stocks all rallied.

The upside CPI surprise, combined with hawkish comments from St. Louis Federal Reserve Bank President James Bullard, sent short-term rates racing higher on Thursday, resulting in a flattening of the yield curve. The two-year U.S. Treasury note yield reached its highest level since January 2020 Meanwhile, the benchmark 10-year U.S. Treasury note yield surpassed 2.00% for the first time since the summer of 2019.

Europe

Shares in Europe rallied, buoyed by strong corporate earnings. In local currency terms, the pan-European STOXX Europe 600 Index ended 1.61% higher. Value-oriented stocks and those in cyclical industries fared well, reflecting inflationary pressures and the possible implications for key central banks' monetary policies.

Core and peripheral eurozone government bond yields rose on the higher-than-expected inflation forecast issued by the European Commission (EC) and an upside surprise in U.S. inflation. UK gilt yields increased after data indicated that the economy contracted less than expected in December and grew 1% in the fourth quarter. This resilience appeared to contribute to market expectations for the Bank of England to increase interest rates again.

T.RowePrice market update

Top 5 things to watch out for in the week ahead:

1. **Geopolitical tensions:** Wall Street's three main indexes closed sharply lower on Friday after the White House warned that a Russian attack on Ukraine could begin any day. While stocks got hit, prices for Treasuries, the dollar and other safe-haven assets, such as gold rose. Crude prices also surged as the prospect of sanctions on Russia, a top producer, added to fears.

2. **Fed minutes, speakers:** With markets already pricing in a strong chance the Fed will hike rates by half a percentage point at its upcoming March meeting, Wednesday's minutes from the Fed's January meeting, will be scrutinized for any indications on how big a move officials are contemplating.

3. **U.S. economic data:** Markets will get an additional update on inflation with Tuesday's release of producer price inflation which is expected to remain elevated. Wednesday's data on retail sales will also be in focus this week. Retail sales are expected to have risen 1.8% last month, boosted by higher auto sales. The economic calendar features reports on industrial production, initial jobless claims, existing home sales, building permits and housing starts.

4. **Earnings:** Earnings season is drawing to a close, but this week will see a big flurry of notable reports. Airbnb Inc (NASDAQ:ABNB) reports on Tuesday, followed by semiconductor giant NVIDIA (NASDAQ:NVDA) and Cisco Systems (NASDAQ:CSCO), which are both due to report after the close of trade on Wednesday.

5. **U.K. data:** It's a packed week on the U.K. economic calendar with the latest jobs figures out Tuesday, inflation data on Wednesday and retail sales on Friday. The Bank of England delivered the first back-to-back rate hikes since 2004 amid surging inflation, which it expects to peak above 7%. Markets are currently pricing in another 130 basis points in hikes before the end of the year.

Index	04/02/2022	28/01/2022	31/12/2021	Week/Week	Year-to-Date
NASDAQ 100	34,738.06	35,089.74	36,338.30	-1.00%	-4.40%
S&P 500	4,418.64	4,500.53	4,766.18	-1.82%	-7.29%
NASDAQ 100	14,253.84	14,694.35	16,320.08	-3.00%	-12.66%
FTSE 100	7,661.02	7,516.40	7,384.54	1.92%	3.74%
Euro Stoxx 50	4,155.23	4,086.58	4,298.41	1.68%	-3.33%