INCLINE
Investment Management, LLC

State of the Market

With Jakub Rehor

Financial and commodity markets spent the week digesting the implications of the coronavirus pandemic.

We have seen a natural experiment in governance and healthcare policy. Several countries took drastic and quick defensive measures and managed to slow down or completely stop the growth in new Covid-19 cases. Those countries include China (outside of Hubei province), South Korea, Singapore, and Taiwan. The measures included school closings, large scale quarantines and curfews, widespread testing, and rapid isolation of patients and all their contacts. These measures are costly and disruptive; they will have negative effect on economic growth; but they were effective in controlling the spread of the epidemic.

Other countries refused to test people widely, were slow to take drastic measures, and downplayed the impact of the epidemic. Leading examples are Iran and Italy. They are both now under extreme stress, with their healthcare systems collapsing and economies in free fall. With the playbook pretty clear, markets can evaluate the impact of current policies around the world and they are marking down prices accordingly.

The US had one month warning time since information about the epidemic became available. We used the time to do what we do best: lecture the rest of the world about human rights, accuse each other of racism, tie up our scientists and entrepreneurs in regulations and red tape, and strut around cockily. What we did not do: test people, quarantine aggressively, and increase hospital capacity. It is now inevitable that the Covid-19 epidemic in the US will follow the path somewhere between Italy and Iran. The final cost of this blunder is unknown; China, which acted decisively once the situation in Hubei got out of control, will probably suffer a one-time shock of 4-5% to GDP (0-1% growth at best, rather than the 5-6% growth expected). The cost in the US will at least match that.

US corporate sector is not prepared to handle a shock of such magnitude. Corporate leverage is at all time highs, fueled by years of plentiful and cheap credit shoveled into the economy by reckless Federal Reserve. Credit spreads were at historically low levels; companies couldn't resist the temptation to borrow to the gills. Most of the cash from loan proceeds was used to buy back shares thus pushing up stock prices and lining up executives' pockets with bonuses linked to stock performance.

Now is the time to be extremely cautious and prepare for tough times ahead.

The Crystal Bay Ubitrend portfolio is in an extreme "risk-off" mode. It is long gold and government bonds. It is short everything else: agriculture, metals, energy, currencies (against the dollar), and, of course, equities. We can expect large counter-trend rallies in the stock market in the near future. Like World War I soldiers charging into machine gun fire, waves of speculators who learned to buy every dip in the last 10 years will come "looking for bargains". Do not join them.

About Jakub Rehor

Mr. Rehor has 20 years of experience in investment management. Currently Jakub serves as the primary portfolio manager and trader for Incline Investment Management, LLC's Crystal Bay Ubitrend Strategy. He joined IIM in 2018. Mr. Rehor is the founder of investment company Ubival where he originally developed the Ubitrend strategy. After working as a business analyst at McKinsey & Co., he started his Wall Street career in 1997 as technology sector analyst with Sanford C. Bernstein & Co. From 2000 to 2004 he worked as equity analyst at Putnam Investments on the team managing the International Capital Opportunities Fund (PNVAX). From 2004 until 2013, he was an analyst and portfolio manager at Third Avenue Management where he was a partner and co-manager of the $1 billion+ Third Avenue International Value Fund (TAVIX).

He graduated from Yale University with a BA in Economics, summa cum laude. He is a CFA Charterholder and holds the Certificate in Quantitative Finance from CQF Institute in London. He has passed the FINRA Series 3 exam.

The Crystal Bay Ubitrend Strategy

Focusing on extreme diversification, the Crystal Bay Ubitrend strategy trades in over 100 different futures markets giving our investors the broadest universe of futures exposure. The portfolio is constructed using risk management techniques originally used in the equity world, with the goal of maximizing diversification of exposures and minimizing tail risk. The investment objective of the CB Ubitrend is to provide the kind of returns early trend followers made a name for themselves with before they became institutionalized and focused on asset gathering. Today billion dollar CTA's are limited by their size to a select number of markets. As a result some of these firms are forced to watch trends develop and sit on the sidelines while smaller managers reap the rewards. The Crystal Bay Ubitrend has a maximum capacity of $100 Million before it meets these same restraints and is currently taking new investors.