



VALOR ASSET MANAGEMENT

March Newsletter 2020

Coronavirus Market Update

The last few weeks have been one of the most volatile periods in markets since the GFC. Valor Asset Management's decisive action has reduced risk for our portfolios and we are positioned for further difficult market movements. It is important to note that our portfolios are still well in positive territory for this financial year which is a decent result considering the Australian stock market is down approximately 14% during this period.

The key positions that we own which are positioned for further market difficulty are as follows:

1. Betashares Strong Bear US Hedgefund
2. Betashares Strong Bear Australian Hedgefund
3. Gold
4. Ishares inflation government bonds
5. Vanguard government bonds
6. Gilead
7. Evolution mining
8. Kirkland Lake mining
9. Cash

1. Betashares Strong Bear US Hedgefund

The Betashare Strong Bear US Hedgefund is up 48% since the market peaked around the 10th of February. This fund tracks between 2 to 3 times the market movement in the opposite direction. We estimate that for every 10% fall in the market we will make around 25% return on this fund. The fund trades daily which can whipsaw the results, however we are comfortable with this risk when the data we are seeing suggests that we are not anywhere near the worst of this crisis.

2. Betashares Strong Bear Australian Hedgefund

The Betashares Strong Bear Australian Hedgefund is similar to the US one, however tracks the inverse of the ASX200 sharemarket.

3. Gold

Gold has not yet risen much in this crisis. With the oil price crashing 31% in a single day this week, we now see the significantly increased risk of a credit crisis. This could likely cause a rush to gold which generally does well in a crisis.

4. iShares inflation government bonds

The iShares Government bond fund invests in Australian government inflation linked bonds. Whilst there has been an irrational rush to buy toilet paper, there may actually be real inflation due to disruptions in the global supply chain. A significantly lower Australian dollar may also increase inflation. By investing into this bond, we have protected a portion of client portfolios against potential inflation risk.

5. Vanguard government bonds

The flight to safety has driven government bond yields to all-time lows. Our position in the Vanguard Government bond fund has performed relatively well under these circumstances. There is talk of negative rates and quantitative easing (QE) in Australia which should increase the prices for Australian government bonds. Additionally, exposure to the government bonds allows us to prioritize capital preservation in these turbulent times.

6. Gilead

Gilead owns a drug called Remdesivir which has initially been proven to work against the Covid19 virus. It is early stages; however it looks like they are winning the race for bringing an antiviral to the market in the coming months. This is yet to be priced into Gilead stock price. There is enormous upside if this becomes the antiviral drug against Covid19.

7. Evolution mining

Whilst the gold price risen slightly due to the Corona Virus, some gold mining stocks have actually fallen providing an opportunity to gain asymmetric upside to a potential gold price spike. Evolution mining has one of the lowest cost gold mines in the world with the Mt Carlton mine. Evolution trades at around 12 times earnings. It has no debt and around \$140million in spare cash making it an attractive position for the current crisis.

8. Kirkland Lake mining

Kirkland Lake Gold has the lowest cost gold mine in the world with its Fosterville mine. It also trades at around 12 times earnings, has no debt and spare cash and should provide reasonable insurance for a credit crisis which could cause a spike in the gold price.

9. Cash

We remain with significant cash holdings. Our current cash balances are near the highest levels they have been since 2011. The aforementioned trades show our present focus on capital preservation and benefitting from market turbulence (via shorts & gold exposure). Our cash holdings conversely are the dry powder we are keeping ready if and when opportunities arise in the coming months.

Further sales in our portfolios:

We took the opportunity today with the small price rises in Smartgroup and Platinum to further reduce risk and sold our positions. The evidence that this is uncontained and the Australian government is behind the curve on stopping the spread is increasing.

When are we expecting to start buying?

We expect to become more assertive and start buying again once we see clear evidence of one of the following:

1. A slowing rate of virus growth
2. Markets offering prices that are near the point of maximum pessimism
3. A virus cure, either through vaccine or antiviral

The virus rate of growth appears to have slowed significantly in China after they locked down over 700 million people. Without these types of drastic measures, we expect it to continue to grow rapidly. So far, the virus appears to be growing unabated.

Markets are not at March 2009 valuation lows. In March 2009, the market cap to GDP in the US was 57%. Today it still stands at around 140%. There is potentially a long way down before we reach the point of maximum pessimism.

Gilead is leading the race for the antiviral, however it will be for another month or two before the results for their trials are released. A vaccine is likely further down the track than the antiviral and is estimated to be anywhere between 9 to 18 months away. We will be watching this space very closely.

We are monitoring the situation extremely closely and will continue to update you with portfolio progress.

I genuinely believe that there will be one of the best buying opportunities coming in the next few months. We are ready to take advantage of what might come and if we are able to allocate to wonderful companies at wonderful prices, we have the potential to grow wealth significantly through this period.

Most importantly, stay healthy and safe. The virus is deadlier than the flu and every precaution should be taken to avoid exposure.

Regards,

Valor Asset Management