ROCKMAN CAPITAL UPDATE

13th March 2023

The year behind & the year ahead

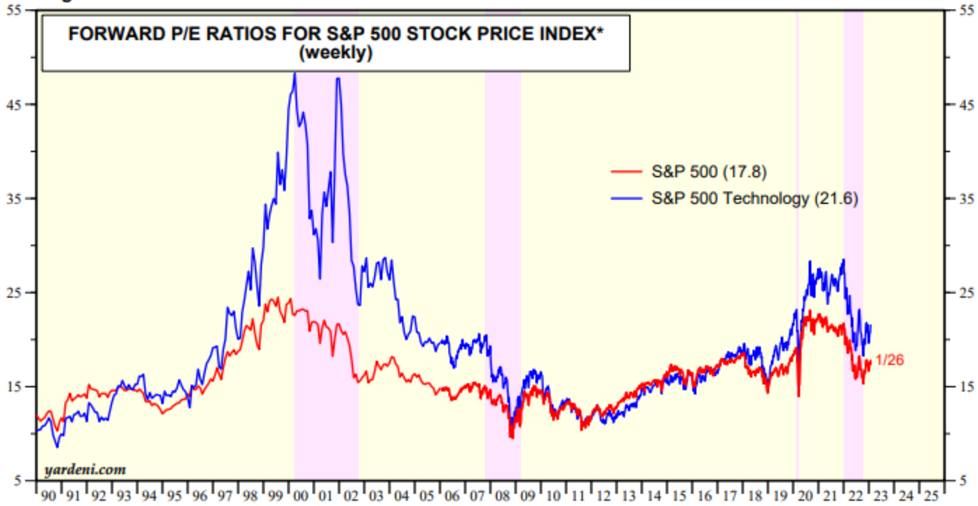
The year behind

2022 was a difficult year for all investors alike. This was owing to many adverse factors including, stubbornly high inflation, aggressive interest rate hikes, COVID restrictions persisting in Asia, geopolitical tensions including the war in Ukraine and ongoing trade tensions between the United States (*US*) and China.

With inflation rates in the US over 7% in January 2022 and rising, it was anticipated that the US Federal Reserve (the *Fed*) would have to act and increase interest rates, to bring inflation into its targeted level of less than 2%. As interest rates rose, we witnessed corporate valuations coming under pressure.

At the end of 2021, Rockman Capital took the view to rotate out of the technology sector by either down weighting our holdings at the time and/or not to allocate further capital to the sector. The graph below, played out to this decision, with the sector derating in 2022.

Figure 15.



* Stock price index divided by forward consensus expected operating earnings per share. Monthly through December 2005, then weekly.
Note: Shaded red areas are S&P 500 bear market declines of 20% or more. Yellow areas show bull markets.
Source: Standard & Poor's.

As indicated above, the average S&P 500 Technology sector P/E, commenced 2022 with a much higher ratio relative to the rest of the US market. With valuations stretched (along with other indicators) and high downside risk, we sector rotated from the technology sector into more defensive equities including, consumer defensives and staples, utilities, and property. Below is an extract of our sector allocation at the end of 2021/22 and 2023.

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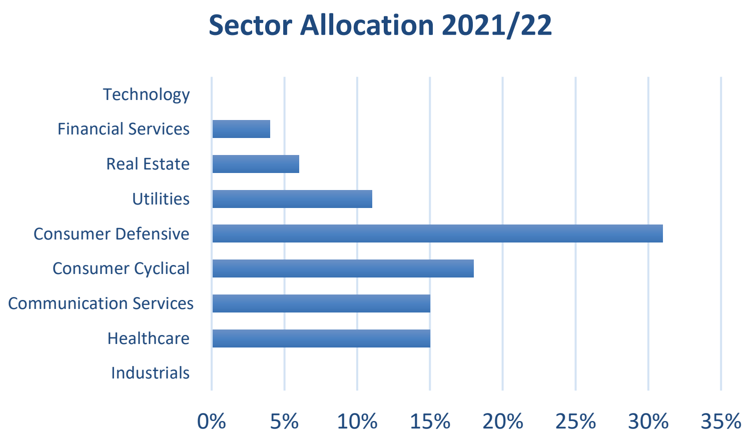

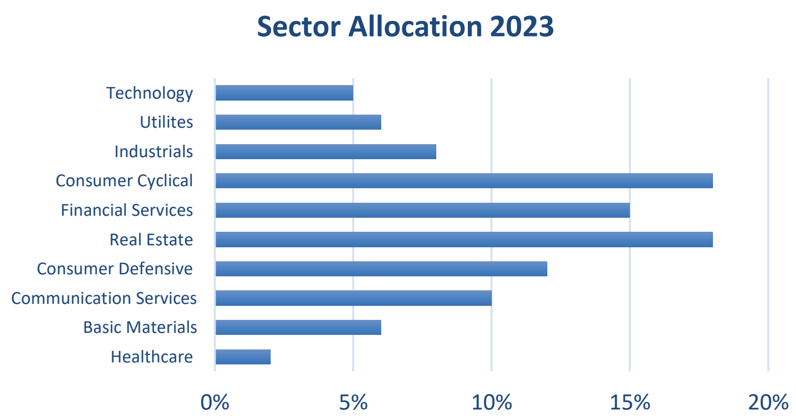

As high-growth stocks came under strain, we decreased downside risk. In our assessment, ICT companies were priced as if they could retain their high profit margins and growth rates. With rising interest rates in 2022 and subsequent sector wide retrenchments and cost cutting, this has not been the case.

In 2023, we have commenced allocating back into the growth sectors. We have further broadened our investment universe to include the sub-sector cybersecurity sector. This is on the back of organizations facing new security challenges to cloud services and remote working, as well as corporate spend on information security in 2022 of more than USD172 billion. Specific investment counters include, Crowdstrike and Palo Alto, both up 16% and 34% respectively year-to-date.

The year ahead

Key factors which are expected to influence our investment strategy in 2023, include:

- The Fed's battle to bring inflation back to its stated 2% target,
- Whether the US enters a recession or not, on the back of rising interest rates,
- Corporate margins (including the sustainability of high levels of corporate debt),
- The Russia/Ukraine conflict,
- Emerging markets, and
- Asset and sector rotation in line with the above.

Moreover, with the outlook for US inflation remaining stubbornly high, it remains uncertain how long the Fed will keep raising interest rates. Many institutions continue to raise their expected terminal rates, to more than 4.75%. The Fed dot plot (See below) indicates only hitting its medium-term interest rate target during 2025.

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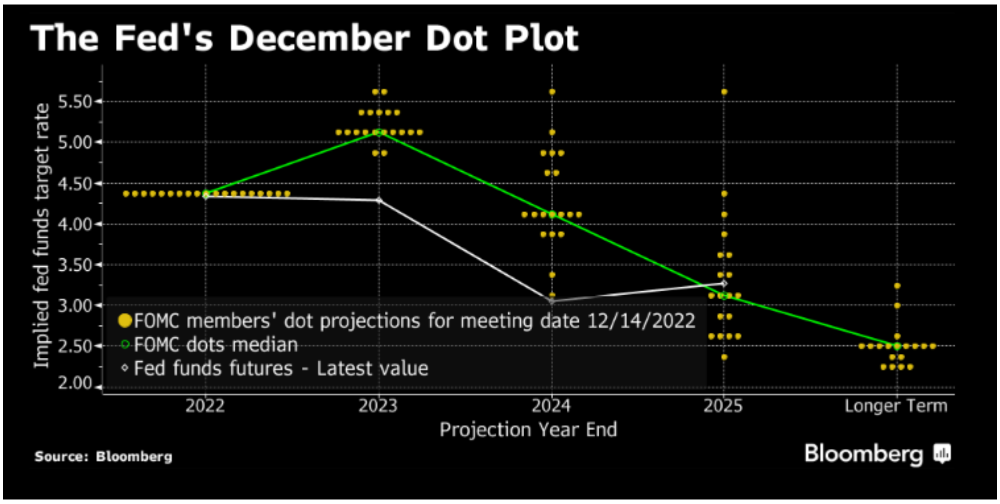
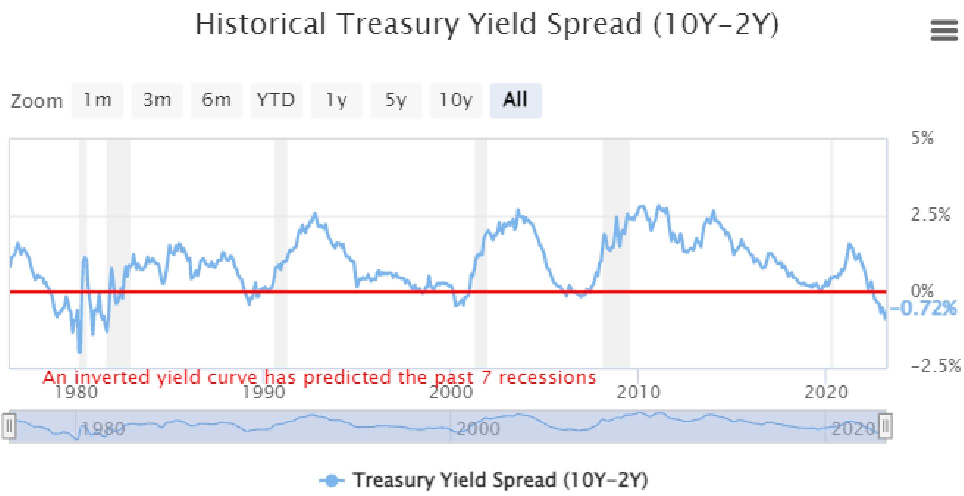


Whilst interest rates remained close to zero, as an investment house, we have had zero allocation to treasuries. This was owing to their negligible return on offer and the significant risk of capital loss once the low interest rate cycle turned.

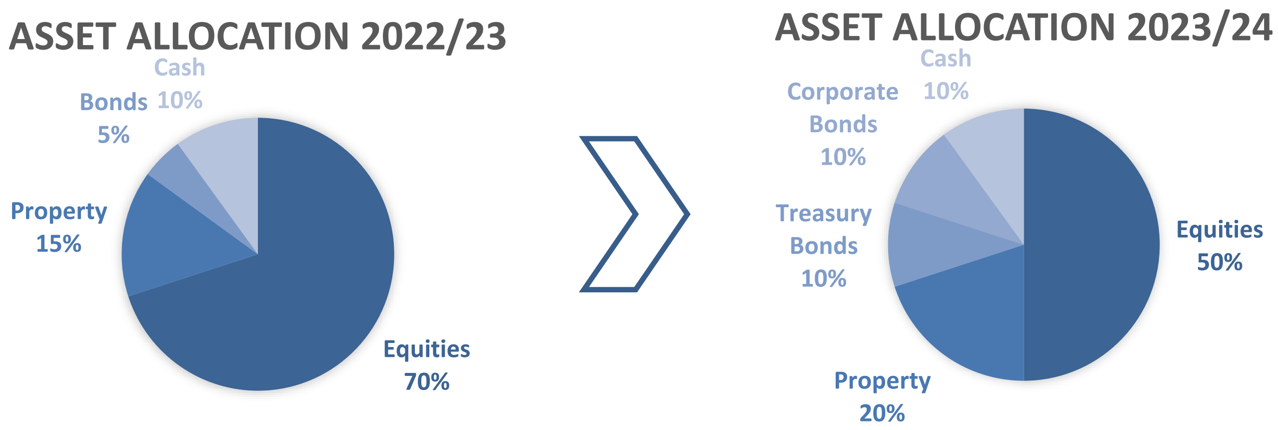
US treasury yield curve remaining inverted since April 2022, the spread has steadily declined to -0,72%, its lowest since the 1980 (See graph below).



As the yield curve has started to flatten and yields rise, we have again started to allocate to treasuries: 1-Year US treasury yields have reached 5%, which is considered attractive for income investors. Albeit, with US inflation presently above 6%, one's real return remains negative. Looking 6-12 months out, we expect to diversify client portfolios further, by increasing our treasury allocations and possible also allocate to corporate bonds too.

Emerging Markets are also an attractive investment opportunity for 2023 due to several factors. These markets have shown resilience during the pandemic, with some economies outperforming developed markets. They also offer high return yields due to their higher risk levels, which can be advantageous in a low yield market environment. They are also one of the most important sectors for consumer spending, especially with travel around Asia picking up. We have seen the luxury goods sector increase over the past few months with LVMH up 13,92% (YTD).

Rockman Capital’s changing asset allocation is indicated below:



2023 is likely to be as challenging as 2022, similarly presenting both a variety of investment challenges and opportunities. By focusing on a diversified portfolio that includes a mix of asset classes, as seen above, we aim to meet client investment needs whilst continuing to manage downside risk. During these times of volatility, it is important to remain disciplined in one’s investment strategy, with a focused long-term approach.

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