THALASSA
CAPITAL LLC

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THALASSA CAPITAL LLC

"It's hard to lead a cavalry charge if you think you look funny on a horse." – ***Adlai E. Stevenson***

While we do not have direct experience in leading cavalry charges, quite often the job we have chosen very much feels like such a dangerous yet potentially rewarding event.

The last two years have certainly felt like such a treacherous but ultimately successful charge. We felt good on our horses (aka our portfolios) and singled out interesting opportunities such as biotech or cyclicals. Certainly, the tricky part is now; our horses need to rest, and perhaps new ones are needed.

The equestrian analogy makes us think about proper positioning in an environment where valuations are high in pretty much every asset class and yet economic opportunities still abound as the world continues to reopen from the darkness of the COVID days.

The current correction is right on time with the typical seasonal weakness and help us mitigate some the valuation excesses we were witnessing in most markets. As expected, high growth and momentum names are suffering more than cyclical and value outfits. This is due to more exaggerated valuations in growth sectors but also because in an economic recovery with rising rates, cyclical and value companies should indeed perform better. To put things in perspective, year to date, value and cyclical indexes have risen between 16% and 17% while momentum indexes have "only" risen by approximately 8%.

Among the cyclicals, energy takes the crown after years of underperformance. This is good news for a portion of our portfolio where we carry positions in energy infrastructures but makes us worry about the future of the economy if an energy crunch develops. Europe is beginning to be squeezed by such an imbalance and that may produce marco economic headwinds. In this context, an allocation to energy would work as an efficient hedge.

We also like commercial real estate, albeit not every name, as an inflation hedge, as a solid and consistent provider of income in a world of still very low yields, and because of its quality collateral.

From a macro perspective, we closely follow the Evergrande collapse in China as an event that has systemic characteristics and yet we find it difficult to equate this evolving situation with the days of the Lehman Brothers' implosion. Evergrande, however, will probably contribute to a long-term slower global economy which might end up generating lower returns compared to the historical averages.

It is in this context that we believe, portfolios today should consider diversification not only among traditional sector and asset classes but also in terms of strategies (options for example) and alternatives where the ability of specialized managers to find returns in less explored markets might help in the new environment.

As always, we would like to thank you for the renewed confidence in our work,

Youri Bujko

Davide Accomazzo