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Research
Forum

The Cut - Edition 88

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Summaries of recent calls:

Manu Bhaskaran - [Centennial Asia Advisors](#) - Asia Macro

Asia after the crisis - [Transcript](#) - [Audio](#) - [Slides](#)

Manu's positive cyclical outlook for the Asian region is driven by the easing of restrictions, massive policy response and business and consumer resilience. He is confident that China's stimulus will be massive (2021 is the 100th anniversary of the CCP) and the spill over into the rest of the world will be powerful. The rigorous approach to the crisis seen in China, Japan, Taiwan, New Zealand and Australia led to a fall in infections and a pick-up in activity. Manu believes restrictions will be eased carefully and sufficiently for the bulk of activity to resume in 3Q20. Therapeutics to reduce morbidity and mortality could be widely available by August/September. Airlines notwithstanding, supply side capacity has been preserved. Chinese oil demand is back to pre-crisis levels, suggesting industrial production has recovered. US retail sales and job market rebound are positive signs. European PMIs for June show a smart comeback. Demand has been supported by a policy response of unprecedented scale and will sustain employment, contain financial risks and preserve production capacity. Monetary authorities across Asia are aggressively cutting rates. This time central banks are letting the exchange rate absorb the brunt of the demand shock. The fiscal response has been sizeable and in addition there are some unconventional policy measures that have taken place - Bank of Korea engaging in QE and the Bank of Indonesia printing money. Manu sees evidence that consumer confidence returned very quickly in China, Japan, Taiwan, Hong Kong and Vietnam. Further, China, Japan, Korea and Singapore have capacity to extend policy support. Longer term Manu sees a number of headwinds for the region: globalisation turning to slowbalisation - a slower expansion of trade, investment, tourism, capital, higher savings rates, and bigger swings in capital flows and higher frequency of financial stresses due to QE and related policies. In terms of supply chain reconfiguration, Manu expects Vietnam, Malaysia and Thailand to be the main beneficiaries. Late comers, India and Indonesia, will find export-led development difficult to pull off. The big risk is Geo-Politics. Here Manu is bearish and expects the US-China rivalry to deform politics in Asia for a long time to come. China is determined that the US vacate the Western Pacific. The US will not leave. Taiwan is in the crosshairs and the military might being built will, in Manu's estimation, be sufficient for China to reunify the island this decade as the US abandons Taiwan without a fight.

Keith McCullough - [Hedgeye](#) - Global Macro

Depression to recession, not recovery - [Transcript](#) - [Audio](#) - [Slides](#)

Keith talked us through Hedgeye's 3rd Quarter Macro Themes presentation in which he discussed their Quad based rate-of-change approach to asset allocation and risk management. There is a huge mismatch between what the markets are saying and what Hedgeye's models are showing. The US economic cycle peaked three quarters after the global cycle peaked in 3Q18 which is when they made their first Quad 4 (slowing growth and decelerating inflation) call in 4Q18. The virus emerged as an exigent shock, but fragility left the cycle susceptible to any catalyst. We headed into deepest Quad 4 in 2Q20. Now Keith believes that the US economy is transitioning to recession stagflation, essentially from depression to recession, but certainly not recovery. He showed that the profit cycle is about to slow to the deepest point and believes an epically negative earnings revision cycle will commence in Q3. We came in to this super pro-cyclically levered in 4Q19, profits were already negative YoY, so it was already late cycle which is why we saw corporate bond bubbles and many other bubbles. We are trying to solve a leverage problem with yet more and more leverage. 60% of companies have already spent half of the government bailouts. 75% of small businesses said they could not survive 4 months with no revenue and now we are at the 4-month mark and COVID is back! Surely, thousands of bankruptcies are around the corner? It is going to take a very long time to sort everything out. The list of data points that Wall Street pumps up to offer hope are misleading. To be confident in a recovery, focus should be on YoY figures - which are deeply concerning, not sequential numbers.

In terms of recommendations, Keith believes stocks will enter bear territory or even crash mode. He recommends shorting the Russell 2000 - not the S&P 500 as they like REITs and Utilities which are bond proxies. Long Energy, Gold Miners and Short Financials, Private Equity, High Yield and Healthcare. Biggest allocation to Treasuries, TIPS and Gold. Long IG Credit since bond issuance over the first six months of this year is bigger than any full year over the last decade. They think that inflation will accelerate, therefore they are short the dollar and long commodities for the first time in a very long time, particularly Ags - Corn and Livestock. Bullish Emerging Markets but very selectively including China, Russia and Indonesia. Short Spain and Italy equity markets.

Macro Research

Inflation outlook: Why are views so diverse?

Examines the different opinions on inflation from a selection of prominent economists, academics and investment managers. Even though the probability that global economies experience a period of deflation in the short term is close to one, remains extremely concerned that the market is underestimating the

odds of a sudden rise in inflation over the next 12 to 24 months (gov. bonds are pricing virtually no inflation risk in the medium term).

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[Economic Perspectives](#)

Brexit: No extension, no free trade deal

Strategy has changed now the UK has left - pragmatism vs. provocation. De-escalate but flashpoints along the way - no extension will be agreed before 1st July and no free trade deal will be agreed by 31st December. The world is moving towards rolling trade deals - supranational co-operation vs. the nation state. COVID exacerbates but does not alter the strategy.

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[Blonde Money](#)

'Something's Gotta Give': US risk-asset valuations are misaligned with reality

Discusses how US equity and credit markets are sending different signals at a time when a wave of corporate defaults is coming and why a pricing reversion is likely to occur prior to further policy response.

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Looking through PBOC policy normalisation

Tightening on liquidity to create room for easing on credit - additional easing measures to support full year credit and TSF growth objectives (and hence real GDP growth) have been delayed, not dismissed. Expects PBOC to resume easing efforts in July.

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Japan: A big winner in the post-COVID cycle

Expects the global pandemic will lead to sustained global fiscal stimulus, backstopped by central banks and hence higher nominal growth through the next expansion. Japan is ideally placed to benefit - relatively cyclical, corporates have reduced their financial leverage and the financial sector will benefit if higher growth leads to the BoJ permitting higher bond yields. Oh, and the market looks cheap!

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US: Excess liquidity around bear markets



Excess liquidity is money growth minus economic growth. Typically, after a bear market starts, it takes time for the Fed to increase liquidity. But this time around, the liquidity response was extremely fast. Coming at the same time as a deep recession has meant excess liquidity has surged. This makes it very difficult for risk assets to sell off by a big margin.

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[Variant Perception](#)

US & China: The Phase One trap

President Trump has maneuvered himself into an awful political trap with the Phase One trade deal. The overhanging risk for markets is that if he can't talk his way out - which looks increasingly unlikely - he may have to blast his way out.

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Unprecedented challenges for the UAE economies

Low oil prices since 2014 has put the petrostate economies of the Arabian Gulf region under severe strain. On top of this, COVID has now brought an abrupt suspension to regional tourism and foreign investor confidence has suffered resulting in a record shortfall in investments and fund inflows. Dubai to require another bailout from Abu Dhabi?

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Sweden's contrarian COVID strategy backfiring?

Cascend's real-time data shows Swedish Q2 economic activity as only slightly better than Italy, Spain and the UK, but worse than Germany, Switzerland,

Netherlands and Belgium. The interconnectedness of global supply chains has reduced any economic benefit that they might have seen and now they must deal with the highest daily death rate per capita of any country globally.

Cascend Securities make direct, real-time hourly measurements of economic activity in a wide range of countries, enabling them to provide analysis months before government data is released.

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Company & Sector Research

— Europe

HY special opportunities...1:1 calls available

How to think about debt purchasers after COVID-19. Discussing general industry characteristics and trends as well as common vs. mythical risk exposures in the balance sheets. How to interpret LTV, EBITDA, bridge to Cash Flows and concludes on solvency. Highlights a long/short opportunity in two of the largest debt collectors, **Intrum** and **Lowell**.

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EMEA Banks: A downward spiral

Looks in detail at the sector's exposure among global active managers. Allocations have fallen to the lowest level on record; saw the 2nd largest decline in ownership across all regional industry groups (behind US Oil & Gas) over the last 6-months. Netherlands and UK have borne the brunt of the selling. Largest fall in funds held: **ING Group**, **HSBC**, **Svenska Handelsbanken** and **Erste Group**.

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JD Sports (JD LN)

Consumer Discretionary

The stock has risen 110% since StockViews closed their original short call, but they believe COVID has only accelerated structurally negative trends. Increasing threat from DTC approach of **Nike** and **Adidas**, while JD's smaller stores and high sales density make it particularly sensitive to lower footfall in a socially distanced environment. 45% downside.

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Boostheat (BOOST FP)

Industrials

A start-up developing a high-efficiency hybrid gas boiler. By highlighting energy savings and ecological arguments, the company has convinced many individuals to order its boiler. However, French small-cap specialists, LPE Research, fear that BOOST, which burns more than €15m p.a. will not realise its business plan and will soon have to increase its capital. TP €2.5 (64% downside).

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Sanofi (SAN FP)

Healthcare

About to enter a new era of soaring margins and teens EPS growth. 3 deep-dive analyses on Dupixent, Flu vaccines and a bottom-up margin analysis show that consensus is underestimating the >600bps margin uplift SAN will enjoy. TP raised to €120 (but M&A offers additional upside).

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— North America

The coming IPO renaissance

Examines the key takeaways from past IPO recovery cycles, showing how IPOs perform best right after slow periods of deal-making inactivity. The IPO market has significantly outperformed the S&P 500 (by 24.7 points on average) after sell-offs. For access to the report click [here](#). Re. specific stocks, Renaissance Capital have recently covered **Albertsons**, **Lemonade** and **Dun & Bradstreet**.

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Canadian Banks: Loan loss provisions, worst is yet to come

Highlights the risk that banks must recognise much higher losses as loans move from Stage 2 to Stage 3. Many investors mistakenly believe that 'lifetime expected credit losses' for Stage 2 loans are the same as provisions taken for

impaired loans. A buying opportunity may emerge when credit losses peak, but for now, Veritas maintains Sell recommendations for all the Big Six banks.

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Retail: Store & corporate ROIC trend analysis; Q2 & H2 forecasts

A combination of COVID and companies suspending guidance means that Street estimates have never been more wrong. Analysts are underestimating the duration in changes in consumer behaviour. Anticipates significant upward revisions of greater than 10% (EPS) to **Sprouts Farmers Market, Dick's Sporting Goods, Lululemon, Target** and **Tractor Supply Co.** Estimates are too high for **Grocery Outlet, Ulta Beauty** and **Boot Barn.**

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[Quo Vadis Capital](#)

Chemicals: Bullish outlook for ethylene-exposed names

Recent moves in oil prices and global ethylene cost curves point to further positive ethylene pricing momentum. Medium/longer-term futures strips point to a continuation of the US ethane advantage. Overweight **Dow Inc** and **Westlake.**

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[Alembic Global Advisors](#)

Industrials: Buy-side idea forum highlights...

Two of the most compelling ideas from MYST's unique idea forum: **Middleby** - heavy insider buying in healthy industry structure (3 leading players); trading at trough earnings on trough multiple. **ServiceMaster** - liabilities are 'ring-fenced' and earnings de-risked; RemainCo severely undervalued post ServiceMaster brands sale.

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Amazon (AMZN) to cash in on dept store spiral: The new bifurcation of retail; luxury is next...

As department stores disappear, sees a future where DTC represents ~75% (on average) and AMZN (or **Tmall**) win most of the third-party distribution for non-luxury brands. In addition, highlights how several premium contemporary

brands are planning to walk away from the wholesale channel entirely and are now looking at AMZN (and even **QVC**) as an alternative.

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[SW Retail Advisors](#)

AMETEK (AME)

Industrials

Expects EPS to double within 5 years based on the value proposition provided by the company's M&A model (proven track record re. substantially boosting acquired companies' margins). Sees EPS above \$7.00 in 2025, resulting in earnings growth CAGR of at least 15%. TP increased to \$125 (39% upside).

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[Gordon Haskett Research Advisors](#)

eBay (EBAY)

Consumer Discretionary

Activist stakeholders will continue to use their outsized influence to urge new CEO, Jamie Iannone, to talk about innovation and technology while seeking a sale of the company. The experience of Iannone, alongside a new Board Chairman, should right the many wrongs of previous governance issues. However, does criticise the CEO's pay package, which bears little performance risk and is imprudently large at over \$41m in value.

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[Management CV](#)

Splunk (SPLK)

Technology

Transitioning to a cloud business. This combined with a period of high M&A and R&D means the market is significantly underestimating ARR growth (\$4.7bn exiting CY2022 and FCF of nearly \$1bn). TAM 10x current revenue. The tailwind of data, security and the convergence in the monitoring market is extremely strong. 47% upside.

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— Emerging & Frontier Markets

LatAm corporate bonds: High quality 'Buy' list

Covering 97 LatAm corporates, credit research provider, Lucror Analytics highlights their top picks - focusing on companies with low business risk, good fundamentals and solid liquidity that will allow them to weather the current global recession and more restricted credit environment. Preferred names include: **Braskem** (BRASKM '50s); **Cosan** (CSANBZ '27s); **Cydsa** (CYDSA '27s) and **Cencosud** (CENSUD '27s).

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A guide to succeed in Asia's \$70bn gaming market

Niko Partners (co-published with **Google**) a comprehensive guide that spotlights new developments, intriguing trends and untapped markets on the rise. The first instalment, 'Play like a girl: Key ways to engage one of Asia's fastest growing gaming audiences', explores how female gamers are transforming Asia's gaming landscape and is (freely) available [here](#).

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C2M / Live streaming trends driving China's e-commerce outperformance

Examines how e-commerce platforms (led by **Pinduoduo** and **JD**) in China are adopting the 'customer-to-manufacturer' model - taking 'just in time' toward 'just in mind' levels of production/inventory optimisation. Expects rapid sales growth given its to target consumers in China's lower-tier cities.

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China's MLCC industry: Excellent opportunity for domestic product substitution

MLCC has great applications in automobiles/NEVs (~20%) and smartphones (+50%), of which sales are estimated to be boosted by 20-30% (5G). Expects a significant recovery in demand following COVID impact and to reduce the price risk from the supply chain, **Huawei** is leading the trend to support the few domestic MLCC manufacturers to expand capacity and strengthen cooperation. Companies set to benefit include **Fenghua** and **Three-circle**.

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Vodacom (VOD SJ)

Communications

'Certainty in uncertain times' - this 20-page report sees Primaresearch upgrade the stock (previously Sell-rated), highlighting the defensiveness of the sector, strong B/S, diversified revenue stream and ROE profile. Expects regulatory risk to be muted over the medium term following the settlement with the Compcom in South Africa; pricing competition appears to have settled too. Coverage also includes an assessment of the Ethiopian license opportunity.

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[Primaresearch](#)

Commodities

Gold Sector: SRI / ESG review

Recent industry events such as **Rio's** Brockman 4 incident and **Norilsk Nickel's** Siberian oil spill highlights the value of SRI analysis. GMR has assessed which companies take reporting seriously and has benchmarked the stocks on key metrics - ranking those who consistently score well (**Northern Star, Agnico Eagle, Endeavour**) as well as those with poor reporting (**Dacian Gold, Red 5**) and lower rankings (**Iamgold, Torex Gold** and **Evolution Mining**).

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Make or break for oil & energy

Following a period of consolidation over the next couple of weeks, expects to see further upside from the deep oversold positions that prevailed a couple of months ago. Brent to reach the low 60s USD/barrel (WTI mid 50s) with the US/European energy sectors rising 30-60% on an absolute basis - implying strong outperformance for the oil nexus into mid/late summer at least.

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[The Capital Observer](#)

Upcoming calls:

Barry Knapp - [Ironsides Macroeconomics](#) - US Macro - **Schumpeter's Gale: It's never different this time**

Richard Hokenson - [Hokenson Demographics](#) - Demographics - **Deficits, the Fed and the post-corona outlook for inflation**

Michael Howell - [CrossBorder Capital](#) - Global Macro and Cross Border

Flows - **Global Liquidity: It's a big, beautiful 'V'**

For further details on these calls and all of our events please see our [Events page](#)

IRF works with 230 Independent Research Providers and Specialist Data Providers, which cover all the major Asset Classes, Sectors and Regions utilising a variety of methodologies.

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