

INVICTUS RESEARCH

The Macro Handbook

Strictly Private & Confidential

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SOS! I'm Drowning!

Most Investors Are Drowning!

Drowning in what? Bad analysis? Debt?

Maybe, but that's not the worst of it.

Most investors are drowning in **DATA**. There's so much data out there that people have lost the ability to put it into *context*.

Putting *all* of the economic data out there into context requires the right ***interpretative frameworks***. In the past, those frameworks were accessible only to people who had a blue-chip pedigree and privileged Wall Street mentorship. Now you have Invictus!

At Invictus, we are your *guide* through the markets. We show you exactly how all the best fund managers in the world think about the economy and the markets.

Our Investment Philosophy

Our Growth and Inflation Framework

There are essentially just two variables that drive the liquid asset markets:

- ***Growth*** – The year over year rate-of-change in economic activity. It can be measured in many ways (retail sales, industrial production, PMIs, etc.), but the most comprehensive and commonly sited statistic is real GDP.
- ***Inflation*** – The year over year rate-of-change in the cost of goods and services. As with growth, it can be measured in many ways, but the most common way is the Consumer Price Index, or CPI.

Everything else is either a) noise, or b) an input into our growth/inflation outlook.

Rate-of-Change, NOT Absolute Levels

For the purpose of forecasting asset class returns, we are far more interested in the *rate-of-change* in growth and inflation than the absolute level.

Our Investment Philosophy Part II

The Growth and Inflation Framework

So, we've established two things:

1) Growth and inflation drive asset-class returns. That's it.

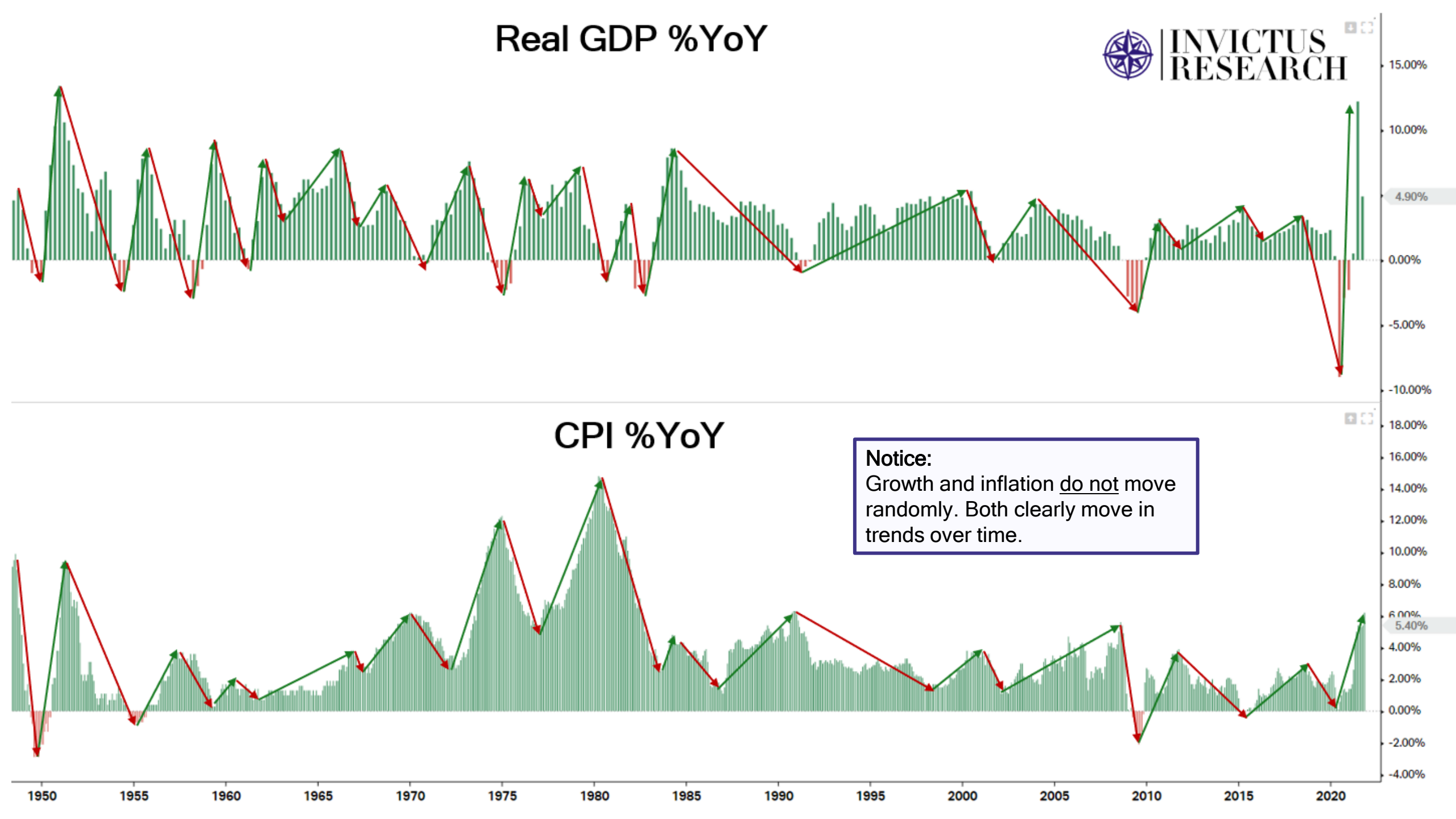
2) The year-over-year rate-of-change matters more than the absolute levels.

But can we predict growth & inflation? Does that entail complex forecasting techniques?

The answer is **NO**. Growth and inflation are predictable because they are cyclical. If something is cyclical, it moves in trends. And trends are, by their nature, predictable.

Together, the trends in growth and inflation form what's called the "business cycle".

Look at the year-over-year rates-of-change in growth and inflation as far back as the 1950s (next slide). What do you notice? *Trends!*


Real GDP %YoY
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15.00%
10.00%
4.90%
0.00%
-5.00%
-10.00%
CPI %YoY
Notice:
Growth and inflation do not move randomly. Both clearly move in trends over time.
18.00%
16.00%
14.00%
12.00%
10.00%
8.00%
6.00%
5.40%
4.00%
2.00%
0.00%
-2.00%
-4.00%
1950
1955
1960
1965
1970
1975
1980
1985
1990
1995
2000
2005
2010
2015
2020

Our Investment Philosophy Part III

The Four Economic Regimes

You may have noticed that the trends on the preceding slide create the possibility of four distinct economic regimes:

	Growth	Inflation	Historical Equity Performance
Early Recovery	↑	↓	Excellent
Reflation	↑	↑	Excellent
Stagflation	↓	↑	Moderate
Deflation	↓	↓	Poor

Our Investment Philosophy Part IV

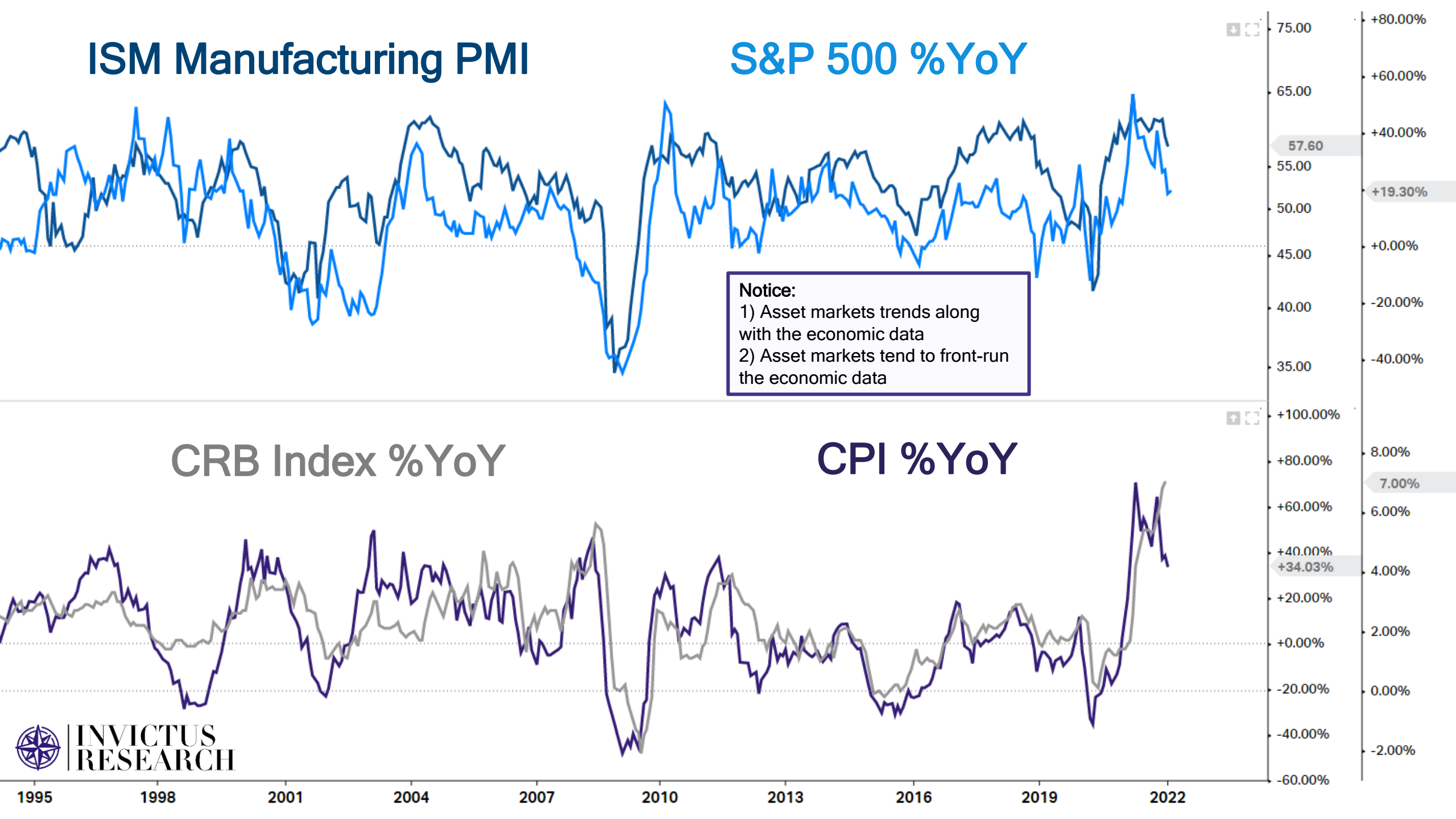
But How Does This Help Me Make Money?

To make money, we need to establish a relationship between markets and the economy. The most important tenets of that relationship are:

1) The market is a reflection of the economy: Because the economy moves in trends, so do the asset markets (see the next slide for proof).
2) All asset markets are, in varying degrees, responsive to growth and inflation (see the slide after next). As such, the asset markets respond in similar ways to similar economic regimes.

For example, through virtually all historical reflations, small caps, energy stocks, regional banks, and commodities have outperformed. Why? Because through each reflation, those assets were responding to the same (or similar) economic realities.

So, in theory, when you expect the dominant market regime to be reflation, you should go long/overweight *reflationary* assets and go short/underweight *non-reflationary* assets.


ISM Manufacturing PMI
S&P 500 %YoY
Notice:
1) Asset markets trends along with the economic data
2) Asset markets tend to front-run the economic data
CRB Index %YoY
CPI %YoY
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75.00
65.00
57.60
55.00
50.00
45.00
40.00
35.00
+80.00%
+60.00%
+40.00%
+19.30%
+0.00%
-20.00%
-40.00%
+100.00%
+80.00%
+60.00%
+40.00%
+34.03%
+20.00%
+0.00%
-20.00%
-40.00%
-60.00%
8.00%
7.00%
6.00%
4.00%
2.00%
0.00%
-2.00%
1995
1998
2001
2004
2007
2010
2013
2016
2019
2022

Our Investment Philosophy Part V

Equity drawdown risk moves left in most developed markets (w/ slower growth/inflation)

Slower Growth ⟵ **Faster Growth**

Gold
Quality
DXY
Long Duration Treasuries
Low Beta
Large Caps
Staples
JPYEUR
Growth
Technology

Small/Micro Caps
Crypto
Value
ZARUSD
Risky Credit
Energy
High Beta
AUDUSD
Industrials
Consumer Discretionary

Slower Inflation ⟵ **Faster Inflation**

Short Duration Treasuries
Growth
Healthcare
Technology
USDRUB
Consumer Staples
Cash
Large Caps
EURNOK

Value
Crypto
CADUSD
Miners
Commodities
TIPS
RUBUSD
Energy
Copper
Real Estate
Base Metals

Risk appetite and liquidity are both *usually* procyclical with growth *and* inflation

Equity Sector Backtest (Stack Rank)

Faster Growth

"Early Recovery"		"Reflation"	
Technology	10%	Financials	13%
Consumer Cyclical	8%	Industrials	12%
Communications	8%	Basics	10%
Healthcare	8%	Energy	8%
Industrials	6%	Technology	8%
Basics	5%	Consumer Cyclical	8%
Financials	4%	Communications	7%
Energy	4%	Healthcare	7%
Real Estate	4%	Real Estate	4%
Staples	3%	Staples	4%
Utilities	3%	Utilities	4%

Slower Inflation

Faster Inflation

Consumer Staples	3%	Healthcare	8%
Healthcare	3%	Real Estate	6%
Real Estate	3%	Basics	5%
Utilities	2%	Energy	5%
Technology	0%	Technology	3%
Consumer Cyclical	0%	Industrials	3%
Communications	-1%	Utilities	2%
Industrials	-3%	Staples	2%
Basics	-4%	Consumer Cyclical	1%
Financials	-5%	Communications	0%
Energy	-8%	Financials	-1%

"Deflation"

Slower Growth

"Stagflation"

Easier Policy

Technology
Communications
Consumer Cyclical
Industrials
Healthcare
Real Estate
Staples
Basics
Utilities
Financials
Energy

Tighter Policy

Equity Style Factor Backtest



"Early Recovery"

Faster Growth

"Reflation"

Easier Policy

Small Cap > Large Cap	Small Cap > Large Cap
Growth Cyclical > Value Cyclical	Value Cyclical > Growth Cyclical
Cyclical > Defensive	Cyclical > Defensive
High Valuation > Low Valuation	High Valuation > Low Valuation
High Beta > Low Beta	High Beta > Low Beta
Low Liquidity > High Liquidity	Low Liquidity > High Liquidity

Slower Inflation

Faster Inflation

Large Cap > Small Cap	Large Cap > Small Cap
Growth Cyclical > Value Cyclical	Value Cyclical > Growth Cyclical
Defensive > Cyclical	Defensive > Cyclical
Low Valuation > High Valuation	Low Valuation > High Valuation
Low Beta > High Beta	Low Beta > High Beta
High Liquidity > Low Liquidity	High Liquidity > Low Liquidity

"Deflation"

Slower Growth

"Stagflation"

Tighter Policy

Small Cap > Large Cap

Growth Cyclical > Value Cyclical

Cyclical > Defensive

High Valuation > Low Valuation

High Beta > Low Beta

Low Liquidity > High Liquidity

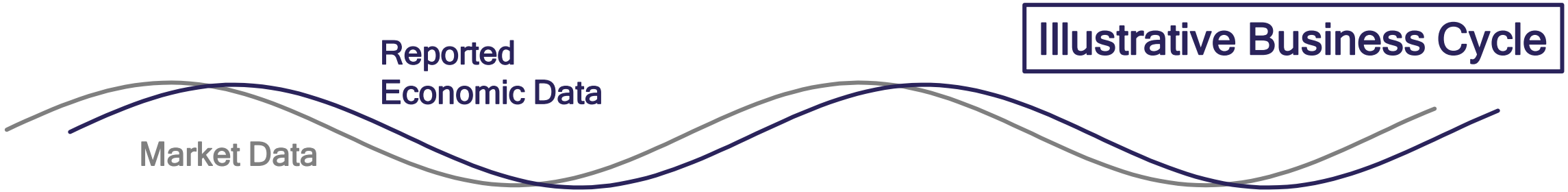
Our Investment Philosophy Part VI

We Want Confirmation from the Asset Markets

Being early is the same as being wrong!

As we've just established, ***the asset markets react in predictable ways to the business cycle***. So, when we see the markets acting a certain way, we can deduce what they are signaling about the business cycle. We will always wait for confirmation from the asset markets (stocks, bonds, commodities, and currencies) before making a call.

The market is *never* wrong about the business cycle. In fact, the asset markets will *front-run* the economic data. Every time. We guarantee it. That's why we pay attention.



Our Investment Philosophy Part VII

Why Analyze Positioning and Sentiment?

"…Non-linear moves in asset prices are largely driven by just two things: liquidity *and* positioning. *As investors, we want to be on the right side of those moves. Or at least avoid being on the wrong side of them. To do that, we need to know when those nonlinear moves might occur. Typically, they occur when the Street is positioned disproportionately on one side of the trade.* ***When positioning is really stretched in one direction, even small counter-consensus surprises can cause big moves in price.*** *Think of it like a rubber band. The further it's stretched, the more violently it will snap-back on a catalyst." [Invictus-research.com]*

We use a number of sources to evaluate positioning/sentiment, including: investor surveys, the CFTC Commitment of Trader's Report, and implied volatility premiums and discounts on front month put contracts.

Put It Into Practice… Try Our Research!

You get…

- Daily updates & analysis on key economic data releases
- Weekly trade ideas
- A monthly deep-dive into how the economy/markets work

Never be caught off-guard by questions about the economy

Make more money for yourself and/or your clients

Develop expertise that will put you in the top 1% of investors

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