Quarterly Call
April 2022

English Version

The Revenge of Geopolitics & Rise of the Old Economy

Quarterly Call Q2 | 2022

Get guidance on investments, and the major structural factors behind your clients' portfolios.

insigneo

Transcribed from comments made during our Quarterly Call Q2 | 2022

April 7th, 2022.

Welcome to Insigneo's Q2 2022 Conference Call, our quarterly get-together with investors, clients, and partners. The world has changed dramatically since we last convened. Our projections have similarly been altered in response to this shifting global landscape, which has arrived sooner than we expected. If the Russian invasion of Ukraine feels to have come quickly on the heels of the Covid pandemic, it seems this way because it has. This is in line with historical precedent as crises tend to beget further dislocations whenever complex systems stumble unto new equilibria.

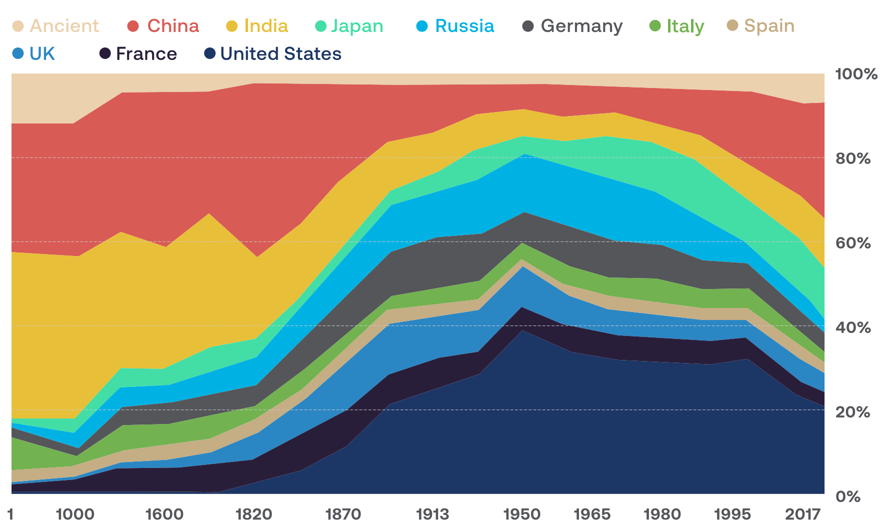
Ahmed Riesgo
Chief Investment Officer
Insigneo Financial Group

The West's internal political divisions were amplified by the pandemic, and global supply chains, particularly in commodities, were mending but not fully healed. Amid this general malaise and perceived weakness, Russian President Vladimir Putin imagined it was an opportune moment to strike in the heart of Europe. But Putin's increasingly autocratic regime is subject to the same fragilities that befall all siloed groups over time. They receive increasingly poorer information, and their decision-making processes lead to greater errors in judgment and suboptimal executions. Furthermore, they do not have the self-corrective mechanisms inherent in consensus-based systems. But Putin's failure to accurately assess Ukraine's domestic resistance, Russia's own military capabilities, and the West's political fragmentation should not be viewed independent of the shifting world order, one we have devoted many pages to here at Insigneo, but as a product of it. Fundamentally, this lies in the United States' relative power decline from a unipolar world that could be shaped largely along its interests and desires.

US's declining ability to orient the world is a result of its decreased share of global economic production due to the rising economic heft of other powers, particularly China. American absolute power has not waned thanks to numerous innate and acquired advantages such as geography, a large and highly innovative economy, strong civic and governmental institutions, the role of the Dollar as the global reserve currency, deep capital markets and its unmatched ability to project both hard and soft power around the world. However, in relative terms, US power has eroded and that should lead to more instability and conflict. To be sure, this does not mean that China will invariably become the global hegemon. Although it is massive, it suffers many structural disadvantages, including autocracy and, most notably, demography. Alarmingly, China will begin an outright population decline much sooner than many projected, and it is not an attractive point of immigration that could mitigate that decline. In fact, Xi Jinping's autocratic rule has made the country less attractive as an immigration destination and has pushed countries in its

From Unipolarity to Multipolarity

Major Global Powers by GDP Reveals US Relative Power Decline and China's Rise



Source: "Statistics on World Population, GDP, & Per Capita GDP, 1-2008". Angus Maddison | IMF

This first chart illustrates more than two thousand years of economic history by comparing the major powers' share of global GDP. It suggests that the

near abroad, like Taiwan and South Korea, to orient themselves further to the West. But the point is that American power has declined, even if it remains formidable – the first among many. As with an asset bubble, while we could not see when *Pax Americana* would end, we could predictably know that it would. And by "end" I mean symbolically, of course, as there is usually a lag between obvious, surface-level observations and the underlying currents that produced them.

Multipolar political systems are inherently more volatile than unipolar and bipolar ones. So, we should expect greater geopolitical risk globally as this shift unfolds. But lest one thinks this means that one should hide in a risk bunker, history tells us otherwise. During World War II, from the day after the Japanese attack on Pearl harbor until Tokyo's surrender in August 1945, the S&P 500 returned 61.5% during that period (13.75% annualized). Switching over to the European theater, if one measures from Nazi Germany's invasion of Poland to its collapse, the index gained 32% (5% annualized). If we are sliding into a new "Cold War 2" equilibrium with realignment along the West, the Eurasian axis of Russia and China, and the rest jostling between the other two poles as before, then history also provides a valuable insight. During the Cold War, broadly defined as 1947 till 1991, the S&P 500 rose more than 2,700% (7.70% annualized) despite enough American and Soviet nuclear missiles pointed at each other to annihilate humanity many times over and several "hot" conflicts along the way. My point is not to suggest that market participants should ignore geopolitical risk. On the contrary, it will have direct consequences on investment decisions that we will address shortly. The core of the argument is that geopolitical risk induces volatility, at first, and then creates opportunities once a new equilibrium is established.

As asset allocators and investors, we must be savvy, not fearful. Decoupling and deglobalization, a trend we believe started in 2008 but has since accelerated, will lead to less productivity with more expensive input costs and higher geopolitical risk. But for as long as human beings inhabit this planet and continue very human-like behaviors such as pro-creating, innovating, producing, and investing, economic growth will surely follow. Certainly, some markets and assets will perform better than others. It is our task to identify them early enough to make a financial profit.

— "The core of the argument is that geopolitical **risk induces volatility, at first, and then creates opportunities** once a new equilibrium is established."

The Beginning of the End for Bretton Woods Implies De-Dollarization

As I mentioned above, we believe globalization peaked around 2008 and has been slowly but steadily declining ever since the Global Financial Crisis. Moreover, the two most recent global events – the pandemic and the Russian invasion of Ukraine – have only accelerated that trend by exacerbating policymakers' reliability concerns when dealing with less-than-friendly state actors. Whether they manifest themselves as US shortages of masks made in China during the pandemic or Russia holding its oil and natural gas exports over Europe's head as it invades European territory, these issues are forcing Western governments to reassess the benefits of the hyper-globalization that occurred during the *Pax Americana*. In other words, they are realizing that the efficiency of the global supply chain may not be worth the trade-offs in both security and stability. On balance, redundancy and reliability of inputs may be worth the cost to consumers of higher prices. All else equal, globalization is a deflationary force, while de-globalization is an inflationary one.

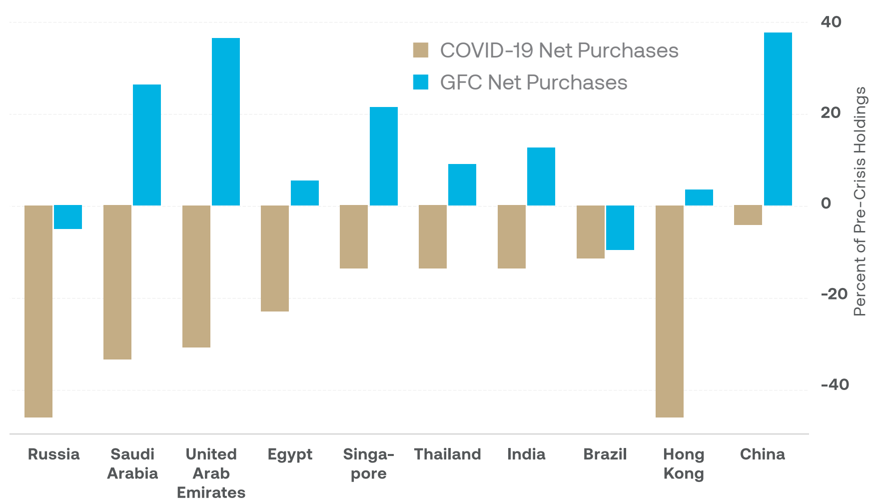
A corollary to deglobalization may be de-dollarization, or the breakdown of the Bretton Woods system where the US dictated the terms of the post-World War II landscape by pinning the US Dollar at the center of the global financial and trading system. The concerns I mentioned around security, stability and reliability are universally reverberating around the world. Non-western governments are also reassessing the trade-offs. Specifically, they are questioning the desirability of the US Dollar as the global reserve currency. As this next chart suggests, unlike during the Global Financial Crisis, many central banks around the world were net sellers of US Treasuries during the Covid-19 pandemic. This disdain for Treasuries was not limited to foes like Russia, but extended to close US allies like Saudi Arabia, the United Arab Emirates, and Singapore. To borrow a Cold War era phrase, even non-aligned nations like Brazil and India, sold rather than bought US government bond obligations. In other words, the demand for US Dollars is waning around the world, among friends and enemies alike.

While Putin may have a made a grievous mistake when he invaded Ukraine, he may not have been the only one that committed an error in judgment, although his is certainly more obvious. However, the Americans, Europeans, and Swiss may too have committed a major policy blunder, even if a more subtle one that may not be apparent for many years. By freezing the Central Bank of Russia's foreign currency reserves, the West has announced to the rest of the world that their Dollars, Euros, and Swiss Francs are no good anymore. When the Dollar is weaponized as an instrument of foreign policy, it is reasonable to expect defensive maneuvers.

Of course, the Western retort would be that this sort of pariah status is only reserved for "aggressors" and "enemies." But in the world of geopolitics, your friend in one generation can be a foe in another. Two current and strident allies of the US were our main enemy combatants in World War II – Germany and Japan. Eighty years is a long time, but central banks should have the long view when deciding where to place their country's surpluses. Another issue that looms against the demand for Dollars is the US's deteriorating fiscal position. American fiscal deficit spending because of the pandemic reached 25% of GDP. In Europe and China, those figures were much lower, 15% and 5%, respectively. According to IMF forecasts, structural

Your Dollars Are Not Good Here Anymore

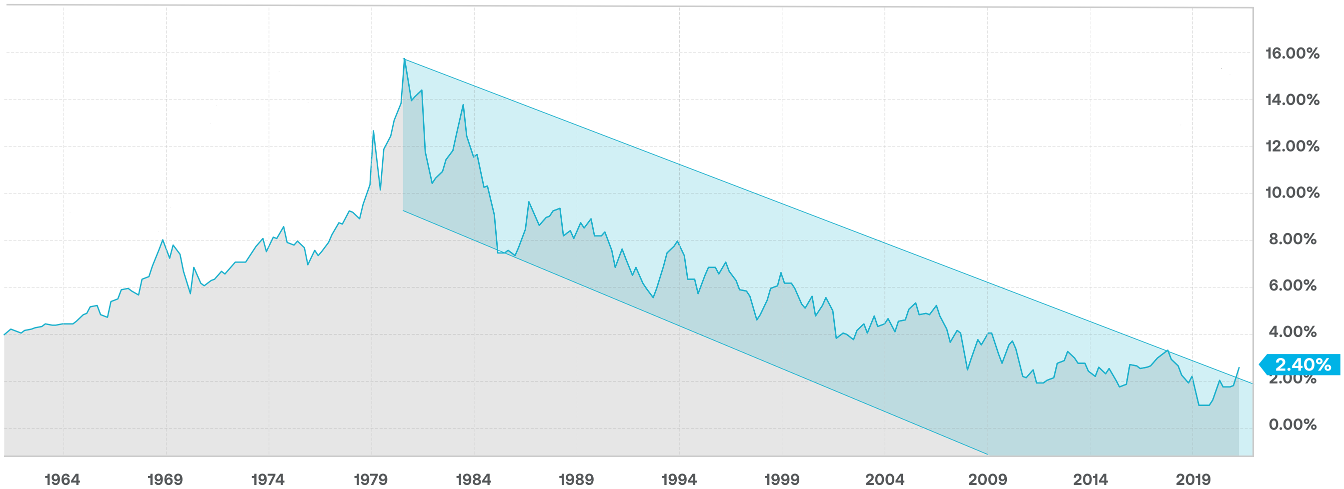
COVID vs. GFC Purchases of US Treasuries Among "Friends" & "Foes"



Source: Weiss, C.R., (January 28, 2022) "Foreign Demand for US Treasury Securities during the Pandemic" FEDS Notes, Board of Governors of the Federal Reserve System.

End of the 40-Year Bond Bull Market? US 10-Year Treasury Yield Hit a Peak of 15.84% in 1981

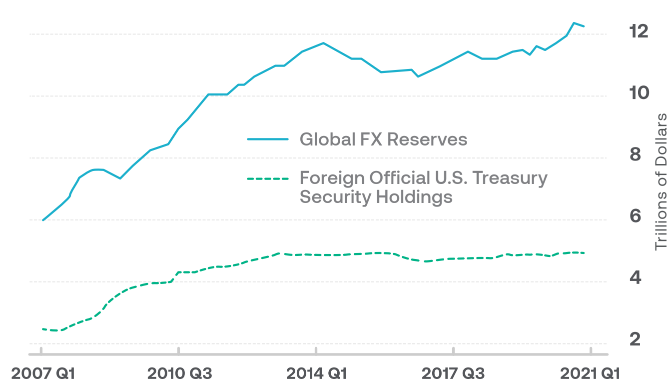
Source: Bloomberg, Insigneo



budget deficits in the country will average 4.9% of GDP until 2026, versus 2% before the pandemic. Over time, persistent budget deficits will reduce savings and ultimately drive the neutral rate of interest higher. A higher neutral rate, in turn, will push bond yields upwards as well. Even though the move up has been quite dramatic so far this year, look for yields to grind higher over the next several years, characterized by successively higher highs and higher lows. Nothing lasts forever and trends always reverse. This chart shows that US treasury yields peaked in the early 1980s amid Fed Chair Paul Volker's inflation-fighting regime and have been making successive lows ever since – lower lows and lower highs. Has this 40-year bond bull market ended? We think this may be likely and would position for a reversal of this Reagan-era trend.

Now, let us be clear, we are not arguing that the US Dollar is about to lose its place as the global reserve currency overnight or even suddenly. It is not easy to dislodge the world's a reserve currency because there is a certain inertia to that standing due to positive network effects. The Greenback's pole position is underpinned by the strength of the US economy, the depth of its capital markets, and the fact that most of the global trade is still settled in US Dollars. As the next chart shows, the level of Dollar reserves has held rather steady over the past five years. In fact, more than 60% of all foreign bank reserves and 40% of the world's debt are denominated in Dollars. But the most important reason it still dominates is that there is no credible alternative out there currently. The European

The US Dollar Has Plateaued as a Global Reserve: Global FX Reserves & Foreign Official Investor Holdings of US Treasuries



Source: US Treasury International Capital Data and IMF COFER

Union is like the US in terms of economic size and the strength of its financial markets, but the Continent has many structural impediments to attaining dominant reserve status, primarily the lack of both a fiscal union and military power. The UK and Switzerland are both too small as a share of global GDP to seriously consider the British Pound Sterling or the Swiss Francs as alternatives. The Chinese Renminbi is an obvious candidate, but China too has issues that prevent this, namely that the country maintains a closed capital account and it is not freely traded. Indeed, the Renminbi only accounts for 2% of global foreign exchange reserves, despite the country approaching a quarter of global GDP. It Is not surprising to read news that the Saudi's are negotiating with the Chinese to settle oil purchases in Renminbi, and the Russians surely are accepting it as payment for their energy exports today to circumvent Western sanctions. Yes, it would be premature to signal the Dollar's demise as it will not yet go the way of the Roman Aureus, the Spanish Real, or the British Pound Sterling until US power wanes significantly from current levels, and that is not likely soon. But we could see a situation where the level of Dollar reserves matches the geopolitical reality we mentioned earlier – the first among many – as the marginal demand for Dollars falls as central bankers continue placing less of their surpluses in Treasuries. In that sense, the most important development over the last few weeks may not be Cold War II, but the first stage of declining Dollar hegemony.

If this thesis holds, US rates will have to go up to entice further buying of Treasuries as they cheapen. The more likely asset bubble, then, exists not in US equity markets but in its sovereign bond market where real yields are still negative despite the recent selloff. As interest rates grind higher, investors would want to own real assets: rental properties, high dividend companies, farmland, agricultural commodities, and industrial metals. "Old" economy sectors like industrials, energy (both hydrocarbons and renewables), miners, and utilities. As central banks around the world purchase and repatriate as much gold as they can, investors would not want to stand in front of that trend either. The precious metal has the added luster of being an attractive geopolitical hedge and outperformer during periods of higher inflation and lower growth. Owning Chinese government bonds is also an attractive option as that, in our view, remains the most attractive bond market in the world. As more trade and reserves settle in Renminbi, it should keep them well bid and it has an attractive carry. Imagine the flows into that market if global reserves rise from the paltry 2% of current reserves to 5% or even 10%. These levels seem conservative in a world where the US has weaponized the Dollar and other countries have taken note.

— "As interest rates grind higher, investors would want to own real assets: rental properties, high dividend companies, farmland, agricultural commodities, and industrial metals."

Global Macroeconomic & Market Outlook

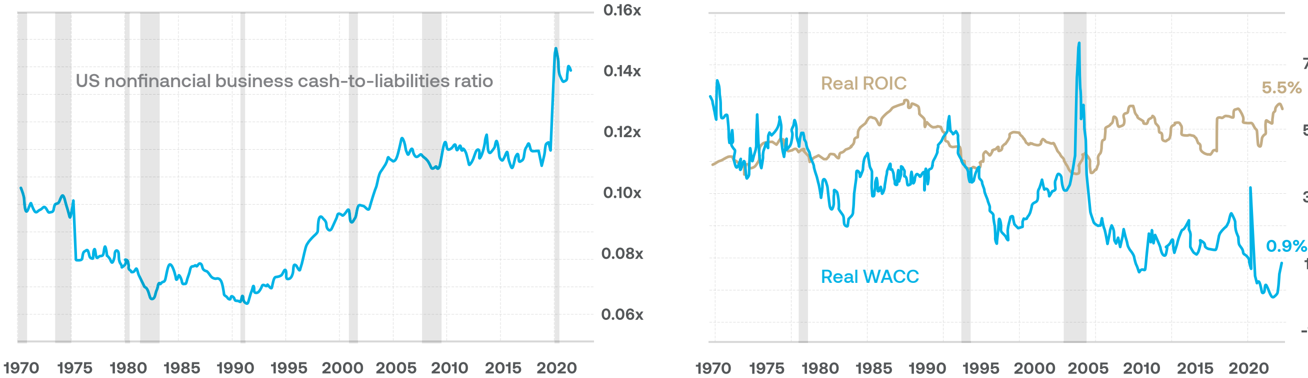
The Russian invasion of Ukrainian has materially impacted the outlook for various parts of the world. The fall in both Russian and Ukrainian exports and the accompanying further strains on supply networks, exacerbated by China's renewed bout with Covid, will increase the risks that inflationary pressures become further entrenched. Moreover, they dampen the growth outlook though that impact should not be spread evenly around the world. In the US with respect to

Insigneo-Forefront Recessionary Indicator: Confidence Measures are Worrisome; Overall, Still Low Probability of a US Recession Over the Next 6 Months | Source: BCA research

inflation, the situation is particularly troublesome as the country was already running hotter due to its extraordinary levels of fiscal stimulus from the pandemic, and rampant growth in the money supply by ultra-accommodative monetary policy. If real interest rates remain this persistently negative for the rest of the year, then inflation rates of 4% to 5% could become more difficult to dislodge. Notwithstanding, we remain cautiously optimistic that the US economic expansion will be sustained even if weakened by the current shock. Our proprietary recessionary indicator, which predicts the probability of a US recession within 6 months stands at only 8.56%, far below the level that would trigger further de-risking but higher than last quarter. As these component parts of the indicator suggest, consumer confidence variables are issuing elevated warnings, market-based indicators are flashing some caution, but the rest of the inputs are relatively benign. This comports with our qualitative assessment of the US economy that, given the health of household and corporate balance sheets combined with tightening but still supportive policies and pent-up demand, a US recession is not around the corner quite yet. We have discussed the sanguine state of private balance sheets in the US for quite some time, but this next chart also reveals that US companies will be able to absorb higher borrowing costs due to rising rates. The cash-to-liabilities ratio is higher than it has been since the 1970s, and the real return on invested capital is still comfortably above the weighted average cost of capital. That means that companies have the balance sheet space to finance their capital needs internally or externally.

— “As these component parts of the indicator suggest, consumer confidence variables are issuing elevated warnings, market-based indicators are flashing some caution, but the rest of the inputs are relatively benign.”

But Companies Can Internally Finance or Profitably Externally Finance | Source: Gavekal



1970s-style stagflation risks have increased, but they are not our base case. The market currently expects 200 bps worth of further hikes for a Fed Funds rate of 2.5% by the end of the year. At this point, the Fed would need to tighten more aggressively to generate a hawkish surprise for markets. In our view, the US central bank will probably tighten in line with current market expectations, or at least not deviate sufficiently from the current path to cause a major market dislocation. Because of this US equites should still generate a real positive real return between now and the end of the year, with Value continuing to outperform Growth. **We have revised down our year-end targets for the S&P 500 from a range of 5000/5100 down to 4700/4900 which is still in line with our expectation back in December 2021** of muted single digit returns in US equity markets, even if certainly on the lower end of that spectrum. For the US 10-year Treasury bond, although we are wary of the recent sell-off and are more neutral on a tactical basis, we still expect it to end the year slightly higher with a range of 2.55%/2.85% up from 2%/2.25% when the year started. These shifts reflect the more aggressive path of monetary tightening in the US due to the war in Ukraine's inflationary impact. It is worth pointing out that most major bond markets outside of China are on course for their worst year since 1994. Instead of acting as buffers to balanced portfolios, they have dramatically increased volatility and losses.

This table summarizes our economic growth forecasts by major region and globally, post the invasion. As you can see, the sharpest downward revision has occurred in Europe which, not surprisingly, is most impacted by the dislocations from the war, especially the Continent's susceptibility to higher energy costs. Please note that these estimates are constructed with two fundamental assumptions. First, that the war does not spill beyond the territorial limits of Ukraine, and it does

Changes in Economic Growth Forecasts*

REGION	PRE-INVASION ESTIMATE	CURRENT ESTIMATE
US	3.25%	2.90%
China	5.00%	4.40%
EU	4.25%	3.10%
Japan	3.50%	2.75%
World	4.25%	3.70%

Source: Insigneo | **Assumptions: Military conflict remains within Ukrainian territory; Russian oil and gas flows continue to Europe.*

— "The largest source of uncertainty, in our view, is that broadening wage pressures in the US labor market prompt the Fed to turn more hawkish than current expectations. The US faces this risk because it is already operating at full employment with an overheating economy."

not broaden into a conflict involving NATO. Second, it assumes that Russian oil and gas flows into Europe remain uninterrupted. If one or both assumptions were to crumble, it would likely trigger a severe recession not only in Europe but globally as well. But it is not our base case, and the last weeks of the conflict have strengthened our conviction behind these assumptions.

The situation in China is a bit more mixed, with strong activity data and potential policy support offset by growing pandemic induced downside risks. As opposed to most other countries, China can afford to maintain its easing cycle since the country faces far fewer inflationary pressures. Our biggest mistake so far this year has been our tactical view on Chinese equities. On balance though and despite their rough start to the year, we believe that Chinese equities could offer a compelling investment opportunity for the remainder of the year if actual policy support matches the rhetoric coming out of Beijing. We also feel confident that China will be able to avoid US and EU sanctions since it will perform a delicate balancing act between Russia and the US/EU. The Western media has overhyped the global scope of sanctions on Russia, as they have largely been imposed only by close US allies. India, for example, continues to trade extensively with the country. Also, it should be noted that in the past China has complied with US sanctions on its own companies, like Huawei, so as not to lose access to Western financial markets. Economic considerations play a bigger role in Chinese strategic planning than they do in their northerly neighbor. With the Party's Congress commencing in October where Xi Jinping will start a new unprecedented 5-year term, we will take them at their word that "stability" is what they most covet this year. However, over the long-term we feel that the investment case for owning Chinese equities has decreased as we would view the lull in regulatory activity this year as a pause rather than a permanent shift. Elevated regulatory risk and the "common prosperity" theme make the country less attractive on a risk-adjusted basis. In addition, China's rapprochement with Russia means that its equity markets may carry a higher geopolitical risk premium going forward.

Risks to the Base Case

What are the biggest risks to our view? The known unknowns? The largest source of uncertainty, in our view, is that broadening wage pressures in the US labor market prompt the Fed to turn more hawkish than current expectations. The US faces this risk because it is already operating at full employment with an overheating economy. As the next chart demonstrates, since last summer US wage pressures have now spread beyond the lowest income segments

Wage Pressures Appear to be Broadening

Source: Goldman Sachs

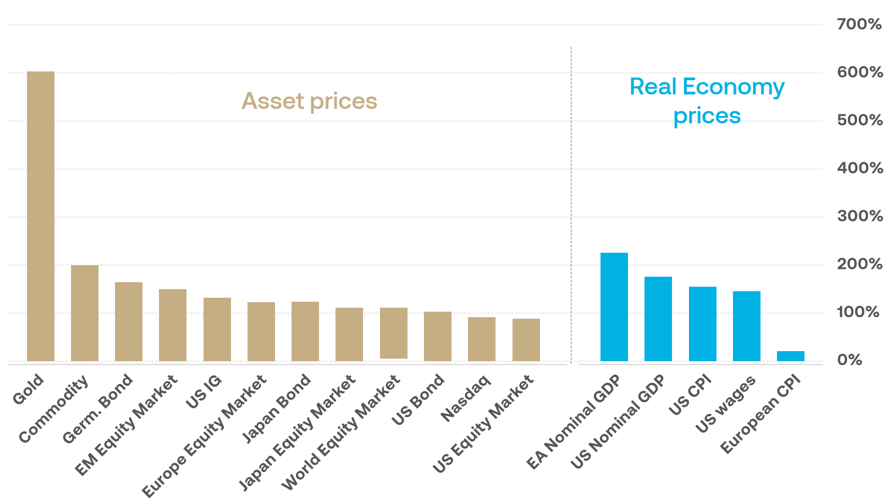
of the labor market into the middle-income portions. Here, one will notice that wages in the second and third quintiles have accelerated versus where they were in July of 2021. Because wages along this part of the distribution are stickier, this increases the risk of a wage price spiral in the US.

Next, are sources of geopolitical risk. I have already discussed the potential pitfalls around the Russian invasion, and they must be monitored diligently because of their high impact. But there are other uncertainties emanating from the Middle East that have, so far, remained outside the headlines. The potential Iranian nuclear deal is placing stress on Israel and some of the Gulf Arab states. For example, Israel and Iranian proxies have been engaging in low-level military skirmishes. There is a risk of further oil disruptions if these confrontations escalate.

Asset Allocation Changes

In general, we are reducing exposure to assets vulnerable to rising yields. The following is a summary of some of the changes we have made to our model portfolios and asset allocation. Given the recent rally in European equities and higher growth risks for Europe stemming from the conflict, including the chance of a mild recession on the Continent, we are reducing our tactical allocation in the region from overweight down to neutral. Within the US, we are further allocating into Value from Growth, lowering the beta of our holdings, and moving into more defensive sectors such as high dividend paying stocks.

Asset Price & Economy Returns From 1973 to 1983



Source: Goldman Sachs

We retain our underweight allocation to developed market sovereign bonds and long duration fixed income. In credit, we are tactically reducing US high yield from overweight down to neutral, increasing emerging market bonds from underweight to neutral, and increasing our holdings of Chinese high-grade credit.

Given increased stagflation risks, we are adding to our current inflation-related investments by initiating a position in high yielding US securities, a US real estate position, and increasing our current commodity-linked investments. It is worth understanding how various asset classes behaved and performed during the last era of low growth and high inflation just in case these risks materialize. This next chart shows price returns from 1973 to 1983, a period in the US when interest rates were high and rising, growth was anemic, and inflation expectations were very elevated. In this environment, gold and commodities were the best performing assets for nearly a decade.

Melissa Ochoa Cárdenas
Investment Strategist
Insigneo Financial Group

Latam, commodities, and the oil giants

Despite the overall difficult global backdrop, Latam markets have been one of the better performing regions around the world due to the importance of commodities within Latin American economies.

Although most commodity-exporting countries have benefited from this landscape, it holds especially true for those that act as substitutes to Russian and Ukrainian exports. Within the region, those countries that should enjoy a boon from higher oil prices are Mexico, Brazil, Argentina, and Colombia, although the first two have more diversified economies. In the case of Argentina, the country reported its highest oil production since the end of 2011, mainly driven by shale oil output. Lastly, Colombia should see higher fiscal revenues from Ecopetrol although there are political risks stemming from the election.

Another sector that should benefit is the agricultural sector, although it entails binary risk for the region. Some countries, like Mexico and Brazil, are net exporters, but they also need to import fertilizers and other inputs for their crops. Significantly, most of those nutrients are imported from Russia and Belarus, which makes them vulnerable to supply chain disruptions.

Petrobras

The Brazilian company reported a relatively positive close for 2021 with higher-than-expected revenues but fell short on expectations for EBITDA, due to higher gas and electricity costs. Sales were derived mainly from higher prices, with the company offsetting lower export volumes and sales in the domestic market. Encouragingly, net leverage reached a new low with net debt-to-EBITDA at 1.00x for 2021.

The trend in increasing tax payments is subject to reversing, as legislation including tax alleviations was passed after Petrobras announced an increase in gasoline, diesel, and gas prices. The Senate also approved the creation of a price smoothing mechanism that establishes price bands, and a fund called the Price Stabilization Account.

Pemex

The outlook for Pemex is quite different. The Mexican government has been aiming to reach self-sufficiency by 2023, exacting a toll on the company.

Pemex reported neutral results for 4Q21, where strong topline figures were partly offset by increases in import costs. Crude export figures decreased on a yearly basis, since Pemex is transitioning away from exporting oil and, instead, focusing on the refinery business. This poses a daunting outlook for the company, as its refinery margin has been consistently falling due to higher oil prices. This makes it more challenging to fulfill refinery needs at the current levels of production. Worryingly, the company's debt profile remains high, and free cash flow was negative again after Q3's recovery. The company is likely going to need further government assistance for operations. Despite the net debt-to-EBITDA ratio falling last quarter, this was due to a liability management exercise done at the end of 2021. It is worth pointing out that Pemex faces debt payments of ~USD 2.6bn and ~USD 4bn for 2022 and 2023, respectively, which make the government's support crucial for the company to fulfill its obligations.

— "Within the region, those countries that should enjoy a boon from higher oil prices are Mexico, Brazil, Argentina, and Colombia. Colombia should see higher fiscal revenues from Ecopetrol although there are political risks stemming from the election.

Ecopetrol

Ecopetrol reported positive results for 4Q21, with higher-than-expected EBITDA and positive surprises stemming from operational and financial figures, as well as a recovery in production. Meanwhile, free cash flow recovered. The balance sheet further improved from positive FX impacts.

Before releasing its 4Q21 results, Ecopetrol presented its long-term strategy and business plan, "Ecopetrol 2040", which anticipates investments between USD 5.2bn and USD 6.0bn annually for achieving sustainability goals.

Nonetheless, the outlook for Ecopetrol looks challenging, considering that the Presidential frontrunner, Gustavo Petro, has sounded hostile to the oil and gas sector. In his campaign proposals, Petro announced that his plan is to gradually transition Colombia from hydrocarbons to renewables. This is a risk for Ecopetrol, despite the company's intentions to be carbon neutral by 2050 and reinforce ESG considerations.

In sum, our takes on the region after taking into account the current backdrop are the following:

- The Russia – Ukraine conflict has benefited some Latam economies, and this positive backdrop has translated into the Latam markets. The commodity exporting economies could benefit further from this backdrop; however, idiosyncratic situations limit the scope of that potential advantage.
- Within the region, there are three main oil companies that could benefit the most from this environment of high oil prices. Each has specific advantages as well as domestic challenges.
  - Pemex looks like the least attractive, considering AMLO's self-sufficiency plan and the halt of Mexican oil exports.
  - If politicians continue to respect the measures taken by the company, Petrobras seems to be safe from additional political noises that could curb the company's performance.
  - Ecopetrol was the first one to take a step towards a greener business strategy, but the political environment in Colombia could undermine this transition. Nonetheless, the importance of Ecopetrol as a source of revenue for the government could allow for its operation to remain relatively stable.

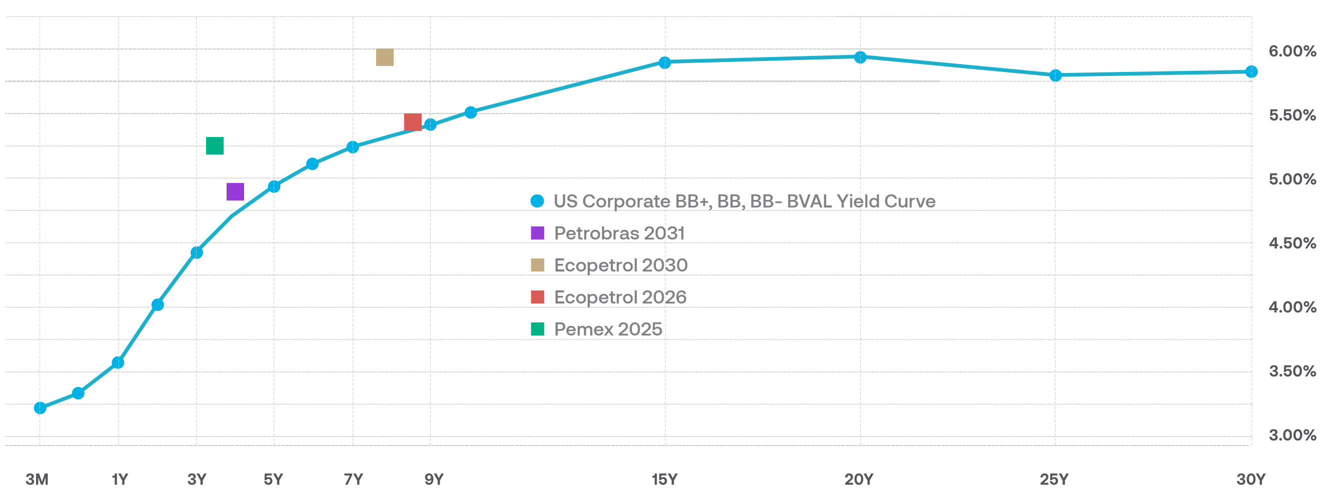
Therefore, we consider the following bonds to be attractive:

- Ecopetrol 2026
- Ecopetrol 2030
- Petrobras 2031
- Pemex 2025

However, it is worth noting that the Pemex recommendation is only for investors with high risk tolerance.

Latam Oil names have tightening space

Source: Bloomberg (as of March 29, 2022)



— "Political risk continue to weigh on the region, specifically for Colombia and Brazil."

The political chapter

Political risk continue to weigh on the region. Let us now take a deeper dive into the outlook of the region, specifically for Colombia and Brazil.

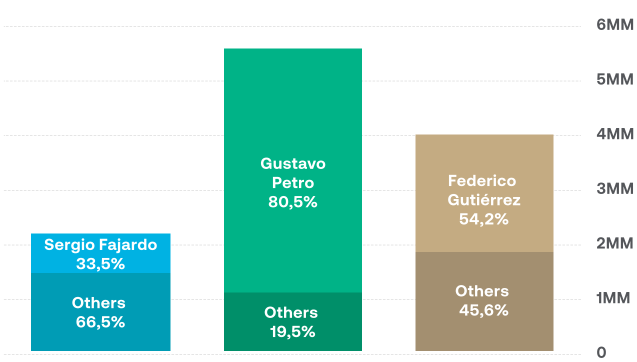
Colombia

First, we will address Colombia. On March 13, Colombians went to the polls for legislative elections and for presidential candidates through party consultations. Those elections resulted in a mixed Congress without a clear majority. Gustavo Petro strongly emerged as the leader as can be seen in the following graph. The center-right Federico Gutiérrez, former mayor of Medellin, emerged as a contender against Petro in a potential run-off. Meanwhile, Sergio Fajardo is faced with the task to unify the center voters who are not convinced by the other options.

Even if the race for the presidency has narrowed, it is still too early to declare a favorite. The debates and additional alliances will be crucial in determining the potential outcome on May 29.
Investors will be closely monitoring the different government program proposals, particularly the changes that Petro is proposing in several crucial issues like pensions, the energy industry, and taxes. Since Colombia has never had a leftist government, it would not be surprising to see investment outflows from international investors. However, the market seems to be constructive on the solid macroeconomic fundamentals of the country, and the carry offered by its fixed income securities. Even with Petro leading, international investors have continued to increase their exposure to Colombian public debt. According to MinHacienda, foreign investors' holdings of TES stood at COP 100tn, equivalent to 24% of the total outstanding, as can be seen here:

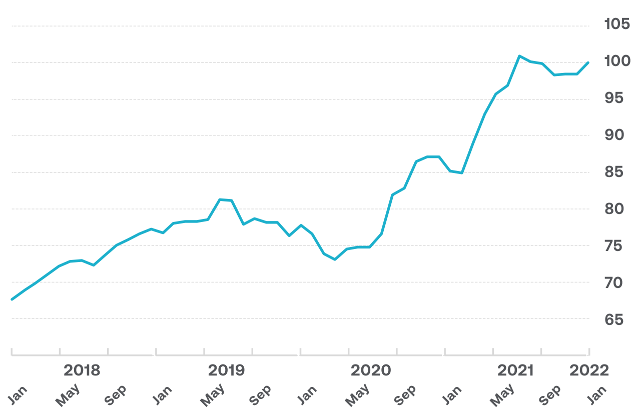
Gustavo Petro consolidated his lead, other winners are trailing

Source: Registraduría Nacional del Estado Civil

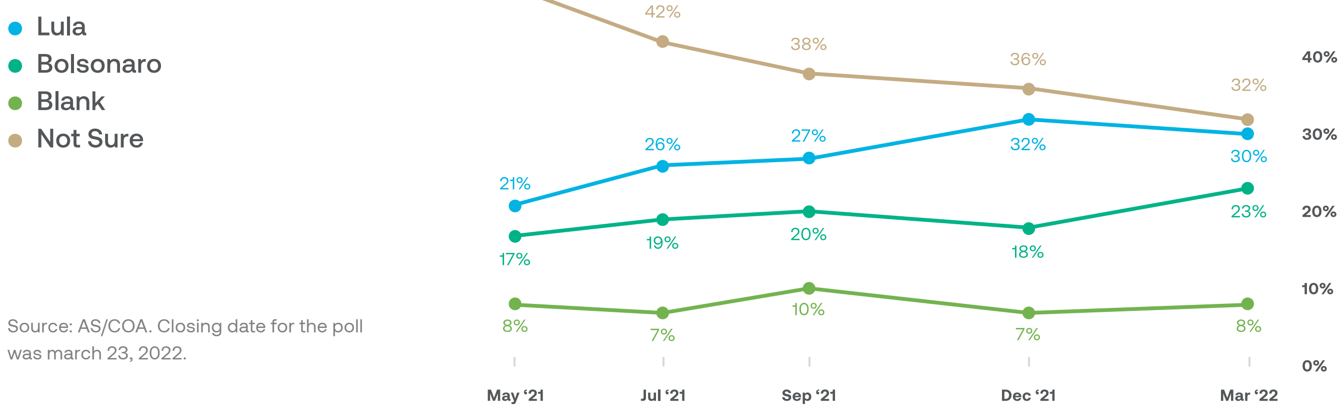


Despite the political volatility, foreigners still like Colombian debt

Source: MinHacienda



Lula is leading the race, but the gap is narrowing



Source: AS/COA. Closing date for the poll was march 23, 2022.

Brazil

Shifting now to Brazil, presidential elections are set for October 2, with the two main candidates emerging from the extremes: current president Jair Bolsonaro and former president Luiz Inácio Lula da Silva. The centrist vote will be crucial given the high rejection rates that both candidates face. If necessary, the two leading candidates will runoff on October 30.
For current president Bolsonaro, the electoral outlook looks troublesome, with his popularity decreasing over the past few months. Among other issues, he has an open investigation on his administration pandemic response. Bolsonaro could increase social spending to boost his electoral prospects, but that could backfire given higher inflation and lower growth.

In the interim, Bolsonaro has been making politically motivated moves, such as ousting his embattled education minister, and replacing Petrobras' CEO after the company decided to increase fuel prices. According to analysts, Lula is expected to portray himself as a pragmatist, which could reduce concerns about his potential victory. Potentially selecting center-right Geraldo Alckmin as a running mate could help moderate Lula's image amid conservatives.

Polls show that Lula is currently leading, although Bolsonaro's numbers have improved lately as the gap narrows.

■

House Views Matrix

	TACTICAL (UP TO 3 MONTHS)	CYCLICAL (UP TO 12 MONTHS)
US Equities[1]	NEUTRAL	OVERWEIGHT
European Equities	NEUTRAL	NEUTRAL
Japanese Equities	NEUTRAL	OVERWEIGHT
Emerging Market Equities	NEUTRAL	OVERWEIGHT
Chinese Equities	NEUTRAL	OVERWEIGHT
US Treasuries[2]	NEUTRAL	UNDERWEIGHT
Investment Grade Fixed Income	NEUTRAL	UNDERWEIGHT
High Yield Fixed Income	NEUTRAL	NEUTRAL
Emerging Market Sovereign	NEUTRAL	NEUTRAL
US Dollar	NEUTRAL	UNDERWEIGHT
Energy[3]	NEUTRAL	OVERWEIGHT
Precious Metals	NEUTRAL	OVERWEIGHT
Cash	OVERWEIGHT	NEUTRAL

[1] Relative to global equities in USD
[2] Relative to aggregate fixed income markets in USD
[3] Relative to an overall commodity allocation

insigneo

Important Legal disclaimer