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ECONOTE No. 114 : Equities: What to invest in now, in the yearend, and in 2024

21/9/2023

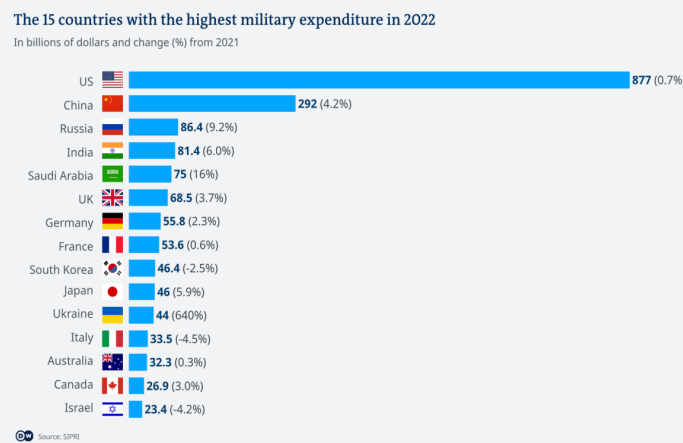
| Summary  | Investment Conclusions   |
|--|--|
| <p>My suggestions what to invest in which sectors and why, appear in the next box: Defence, Renewables and focused Pharma. My suggestion what not to do is to spend time in guessing when will the Fed think that inflation has stabilized and, hence, cut rates. There are two conditions here, stability of inflation and the timing of the cut which allow scores of combinations of data/dates to keep the markets jumpy. Similar considerations apply to the ECB. China's economic malaise is mostly domestically driven and exaggerated by poorly understood debt issues. China can afford a much bigger fiscal deficit which will help fund the rescue of the property sector and thus stabilize the equity market. The longer the Chinese authorities delay concrete and funded details of the announced policy initiatives, the longer the economic malaise will linger. Hence rather than outguess the Fed and wait for China, go for these sectors, one of which, Defence, is interest rate inelastic as its main clients, governments, are not affected by higher rates!</p> | <p>For compliance reasons I cannot name which companies to buy, but only suggest sectors. Neither can I suggest strategies in terms of buy/sell/hold or use of derivatives. Investors will have to rely on their SFC licensed brokers' recommendations. My sectoral call: <b>First</b>, Defence on the basis that since the outbreak of the Ukraine war there has been a big expansion of global, and not just NATO, arms spending which will stay. <b>Second</b>, the COP 28 meeting in Dubai will confirm the road to climate hell we are all in, and the need to invest as much as possible in Renewable Energy broadly defined. <b>Third</b>, Covid is not over by a long shot but Long Covid (LC) is here, will stay and will continue to debilitate millions. Favor Pharma which has long term LC research, both palliative and curative. There is a lot of available information on Pharma firms actively engaged in this area.</p> |

## First the basics and then the sectors

**First**, the reasoning behind considering these three sectors for investment is very simple and is unrelated to the current obsessive and fruitless discussion over the next move in central bank interest rates. All three sectors have behind and in front of them specific events which have already led to massive spending on their products ( Defence ) or will lead to spending in the cases of Renewable Energy and Treatments for Long Covid. **Second**, these are very broadly defined sectors, some with hundreds of companies, especially Renewable Energy. Hence these recommendations are purely sectoral because, as indicated, for compliance reasons I cannot suggest specific companies to invest in. If a sector is doing well, individual companies within the sector might have been underperforming. Hence specific research and advice on individual companies or ETFs must be sought in order to expose portfolios to a sector which is already doing well. **Three**, the reasoning behind the choice of these sectors is simple. **Defence**: the Ukraine war triggered an outburst of defence spending, and across the world including Asia. Concerns, justified or not, over China's expanding global influence has led to defence spending rises in India, S.Korea, Australia and other countries. The data in Fig.1 do not cover the developing trends in 2023 which will see nearly uniform increases. Once defence spending rises it tends to do so over long periods as it is difficult to stop or reverse it because of its long term nature. **Renewable Energy**. The forthcoming COP28 UN meeting on Climate in Dubai Nov.-Dec 2023 will confirm the extent by which the world is way behind the degree of emissions control in order to to achieve the 1.5C

warming level by 2050. It will also focus on the accelerated deterioration of climate in general with the massive fires and floods and in Europe in the hottest summer ever recorded, Libya floods, and the further melting of the Arctic cap. Countries will not agree on the extreme measures now needed and it will fall on the Renewable Energy sector to do as much as panic will permit. So COP28 will simply be the starting bell of spending far more on climate despite the fact that it will still be too late and too little. As for **Long Covid** and **Pharma** see the details and reasoning in the Fact Box.

Fig.1: Defence spending in 2022 and yoy% rise since 2021



## God (and the Devil), is in the details

The data in Fig.2 are supportive of the investment argument presented here. The three indices representing the three sectoral choices, are set against the S&P 500 ( red) index reset at 2022.=100. From the end of 2022 these indices outperform the S&P500, except with Defence ( bl) accelerating and surpassing Pharma (blue), but Renewable Energy tumbled, significantly. The 2022=100 setting was specifically chosen to coincide with the start of the war in



### Fact box : Long Covid

In Econote No. 113 of 11/7/23 I analyzed in detail what Long Covid (CV) is and what are its severe impacts on the health and productivity of the labor force .LC are a series of debilitating symptoms following an infection and recovery from Covid. The symptoms can linger for months and years and, although not all are life threatening, most are debilitating. The popular notion that Covid has now been “cured” and eradicated is totally untrue. Covid is still mutating and infecting millions of people across the world but we do not know about it because most governments have stopped counting and recording infections once all Covid restrictions were lifted. And remember that as long as Covid infects, then some of the infected will very likely suffer from LC symptoms, tiredness, muscle pains, irritability etc. There is universal ignorance over the impact of LC except in the medical, but definitely not in the investment circles. Hence my insistence in drawing attention to its investment implications.

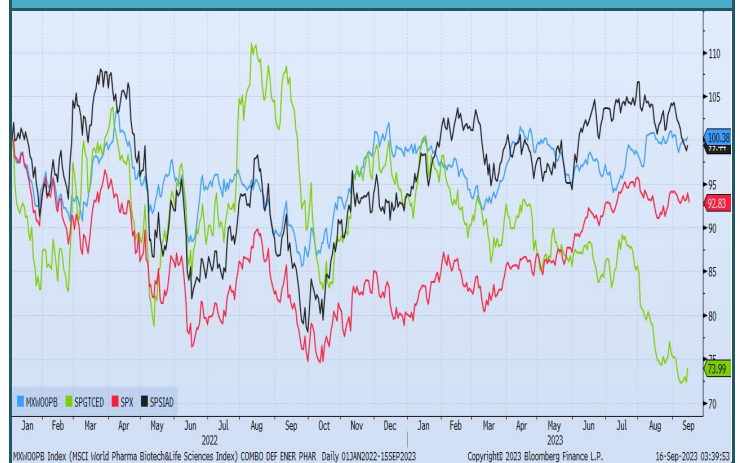
### Evidence on the size and severity of Long Covid (Quotations):

“While Covid 19 rapidly emptied cities and shut industries, LC has been stealthier. Yet its impact in the past two years has been huge. A study by the Washington Univ.School of Medicine and the Veterans Affairs St. Louis , showed the condition is so widespread that the “healthy life years” lost across the population surpassed those of lost to cancer or heart disease.LV took 80 healthy life years per 1,000 residents in the first 2 years of post-infections, compared to 50 for cancer and 52 for heart disease.....The number of sufferers is estimated conservatively at 65 ml worldwide. ( FT 14/9/23). A health life year is the number of remaining years that a person is expected to live at a certain age without the disability in question, here LC.

“Approximately 6.0% of all US adults are currently experiencing LC”(Medscape,29/6/2023).WHO calculated 1.5 ml Covid infections over a monthly period in Jul-Aug.2023, that is about 18.0ml annualised, from which 10.0% could experience LC ,1.8 ml!

the Ukraine and thus gives an undue “advantage” to the Defence sector. Fig.3 which shows a longer-term perspective, that the relative emphasizes that the relative performance of the sectors forms only part of the reason why chose them. Renewable Energy has done relatively well since 2019=100 but less so in the post-Covid period.

Fig.2: Defence (bl),RenewEnergy (gr),Pharma (blu),SPX (red) 2022=100



Source: Bloomberg

## The long goodbye and the summary

The recommendation to focus on the equity opportunities in these three sectors is based on expectation that they will benefit from increased investment flows driven by different reasons. But these must come with two simple precautions. **First**, we use here three sectoral indices to show the performance vs the S&P500. For Defence we use the S&P SPSIAD which covers the major US defence industries only. For Renewable Energy we use Bloomberg’s SPGTCE which covers, among others, 30 Chinese, 19 US, 6 Brazilian and 4 German companies. And, finally, for Pharma we use the MSCI MXWO0PB index covering pharmaceutical companies in 23 countries. There were no specific reason for the choice of **these** particular indices other than their coverage and the reputation of their compilers. Indices cover a multitude of angels and devils and, hence, once the attractiveness of a sector is established by macro developments, policy decision etc and the overall relative performance of the sector is shown, then the important choice of the tactical decision of companies to invest in will take place. We repeat for the nth time here that compliance restricts us from making buy/sell/call on specific companies in each sector. **Second** The calls on two sectors are based on specific and concrete factors. For Defence, is the pivotal turn to massive spending on arms across the world following the start of the Ukraine war. This is added to the existing trend of more defence spending in the Pacific region as a reaction to the perceived China threat. For Renewables, the expected frightening and sobering aftermath of the Dubai COP 28 meeting in Dec. 2023, combined with the fortuitous ( poor choice of words here !) climatic outbreaks in the summer of 2023, and is expected to push, more than ever, investment in green energy. The Long Covid/Pharma call is the riskier of the three as its success depends on two factors (1) An appreciation of how large ,and growing, is the number of people suffering from the symptoms of LC. Add also the possibility of massive underestimation of the true numbers as governments have stopped counting anything related to Covid.(2)Appreciating that Covid is alive and well and infects people by the millions. A confirmation of this will propel more Pharma research in the development of palliatives and curatives for this big and expanding market with long term prospects.