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Hesiod Financial, LLC
Monthly Report

October 2019

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Monthly Overview

Highlights

- At the end of October, the Federal Reserve slashed interest rates by 0.25%, marking the third rate cut since late July. However, Fed Chairman Jerome Powell signaled it will not cut interest rates further unless the economy slowed sharply.
- The Consumer Confidence Index fell from 126.3 in September to 125.9 in October. Consumers' assessment of current business and labor market conditions rose from 170.6 to 172.3, but consumer's short-term outlook for market conditions fell from 96.8 to 94.9.
- Total nonfarm payroll rose by 128,000 in October and the unemployment rate was little changed at 3.6%. Notable job gains occurred in food services and drinking places, social assistance, and financial activities. Within manufacturing, employment in motor vehicles and parts decreased due to strike activity.
- Protests in Hong Kong have dragged the region into a technical recession in the third quarter. The Eurozone's economic expansion continued at a crawl, with little prospect of robust growth. Third quarter GDP rose by 0.8%, same as the quarter prior.
- Boris Johnson agreed to accept the EU's offer to delay Brexit until January 31, 2020 in order to get a Brexit deal done. This heavily contrasts Boris Johnson's 'do or die' promise he repeatedly made earlier in the year.

Market Sentiment

The federal reserve ended the month of October by lowering the federal funds rate by 25 basis points to 1.25-1.50%, in what appears to be the last of the rate cuts. Futures traders now believe there is less than a 50% chance of another rate cut in December. This prediction is largely due to the fact that the United States and China agreed on Phase 1 of a trade deal. The market appeared to remain neutral on the rate cut, while Trump continued his harsh criticism of Chairman Jerome Powell. The 10 and 30 year US Treasury bonds are trading at 1.72% and 2.20%, respectively, which is up from the previous month's 1.52% and 2.02%.

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The financial sector was a strong area for the market and investors in October, as the major banks reported better-than-expected earnings. Goldman Sachs and Morgan Stanley reported strong sales and trading revenues.

Sector Outlooks

Communication Services / Information Technology (CSIT)

October was a great month for the CS/IT sector. We saw a strong recovery from Palo Alto Networks, with the company stock pricing increasing by 9.4%. Our sector believes that this growth will continue for PANW due to the rising need for cybersecurity. We also experienced strong returns from our holdings in the iPay ETF. For the month of October, our sector showed positive returns of 4.75%, outperforming the S&P 500.

Looking towards the future, our sector is currently hoping to capitalize on streaming war, specifically with Disney's new streaming platform. We are also more optimistic about the growth of the Technology sector as a whole due to easing trade war tensions.

Materials / Energy / Industrials (MEI)

Since the beginning of the Trump era, defense budgets in the United States and NATO have been on the rise. Given this global tailwind, we maintain our bullish stand on the Defense sector. With the continued controversy over the Boeing 737 Max. It appears the 737 Max will stay grounded by the likes of American until mid-January. Boeing is facing the lowest annual total orders in the last eight years, as they have logged less than 40 orders this year in comparison to the over 200 orders in the midway point of the previous year. Boeing also announced it will decrease monthly production of 787 aircraft to 12 per month on account of "the current global trade environment. "The shareholders of Raytheon and United Technologies also recently approved of a merger to close in the first half of 2020, making the second-largest defense company after Lockheed Martin Corp. Raytheon recently won a $5 billion contract with the US Government to build a new radar for the Patriot missile defense system; this contract could soften the blow of losing the Lower Tier Air and Missile Defense Sensor system deal. The radar isn't due to be fielded before 2022. While the transaction only accounts for a low percentage of Raytheon's sales, the importance of the broader Patriot system has created an overhang in the company's shares. For United Technologies, strong orders for the company's Geared Turbofan engines and its continuous focus on investment across aerospace products portfolio are poised to drive growth. Within the defense sector, we have found great success trading on Huntington Ingalls. Given the company's niche position within the US defense industry: as the US's sole producer of large-scale combat surface ships and submarines, we see the long-term valuation of HII as relatively stable even compared to the likes of Raytheon. For this reason, we are currently taking advantage of the cyclical nature of HII's stock price. Other areas of particular interest for MEI include Cosan Limited (CZZ), a Brazilian petroleum and logistics company. A new position, Cosan Limited offers a unique exposure both within a growing Brazilian economy and alternative fuels mainly within sugar canes. Moreover, given the joint venture with Shell, Cosan Limited has proven itself to be a major player in the distribution of consumer gasoline. In summary, we believe the clear outlook for Cosan Limited creates a strong valuation play that we will seek to take advantage of closing into this year.

Consumer Goods & Healthcare (CGH)

The CGH group has been relatively inactive in October, solely closing a position in Edgewell Personal Care (EPC) for a large realized gain. Moving forward, CGH will begin to focus on healthcare as opposed to consumer goods, due to both the recent positive trend of the healthcare industry and consumer uncertainty. Many large healthcare firms such as UNH and JNJ beat last quarter's earnings in an increasingly volatile time, and the CGH group plans to take advantage of this positive trend in the coming months. However, the healthcare sector's long-term outlook is still very questionable, with democratic presidential candidates eyeing Medicare-for-all and government-manufactured generics.

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The CGH group will maintain its position in its self-made Retail ETF, now consisting of four large consumer staple positions after the closing of the EPC position. We will also heavily consider closing our position in Constellation Brands (STZ), as it has only been capable of generating a small negative return since opening the position in early July. The unloading of STZ grants more capital for the CGH group to work with, hopefully to be used towards investing in the healthcare industry in the coming months.

REITs / FIG (REIT)

Foreign Exchange (FX)

USD: US manufacturing data continues to signal some trouble. Core durable goods orders fell by 0.3%, the second decline in three months. Its manufacturing PMI improved to 51.5, above the estimate of 50.7, but this still points to minimal expansion. It has seen a depreciation against most major currencies, and with no trade war resolution yet, we expect the USD decline to continue into November.

GBP: Earlier Brexit news gave some optimism about the GBP, but now Brexit deadlines are again on the horizon. This gives investors cause for fear and will most likely weaken the Pound, erasing its recent gains. We therefore predict depreciation on the GBP.

Monthly change: 1.23 → 1.29.

EUR: Despite a relatively solid October, the Euro is poised to drop again; its gains were also mostly because of a weak dollar. The Eurozone economy is still faltering, and like last month Germany showed a sharp decline in exports and manufacturing. Brexit deadlines could cause even more uncertainty for the Euro. We predict a depreciation of EUR.

Monthly change: 1.09 → 1.12.

CAD: The Bank of Canada held its policy rate at 1.75%, breaking away from the global trend of lower rates. PM Justin Trudeau was recently re-elected, but his party has a minority government, which may cause uncertainty for the CAD. Canada has seen a decline in core retail sales for the third month in a row, along with low real GDP growth. Overall, we are neutral on the CAD.

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Monthly change: 0.76 → 0.76.

INR: INR/USD traded relatively flat over the past month. India's economy saw the slowest GDP growth in 5 years, and the central bank, RBI, recently lowered the repo rate by 135bps to 5.15% from 6.5%. From this, we predict a decline in INR.

Monthly change: 0.014 → 0.014.

FX Asia: Much the same story as September. Trump's trade war persists, and so do the effects on global and Asian uncertainty. Most Asian currencies declined, but so did the USD, so the relative valuations weren't affected too much. A slight exception was China: (USD/RMB went from 7.13 → 7.04).

Trading Desk (Kratos)

Kratos closed our Hong Kong short position for a net loss to avoid the risk associated with a Phase 1 trade deal between China and the United States. Although the position was closed at a loss, we were protected against the announcement that came out from President Trump and President Xi. Our largest position is now long the financial sector, where we plan to capitalize on strong earnings from the banks. With no additional rate cuts in sight and the already-low 1.25-1.50% federal funds rate, we see high potential in the financial sector.

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Portfolio Analysis

Performance

	Monthly (%)	Since 7/1/2019	YTD (%)
Hesiod Financial	3.10%	6.18%	-2.22%
S&P 500 Index	3.46%	3.85%	22.72%

Key Statistics

	October 2019	September 2019
Sharpe Ratio	-0.94	-1.06
Standard Deviation of Monthly Returns	4.35%	4.60%
Weighted Avg. Beta	0.99	0.83
Weighted Avg. Market Cap	50 B	64 B
Weighted Avg. P/E	44.22	56.38
Gross Exposure	94.23%	75.88%

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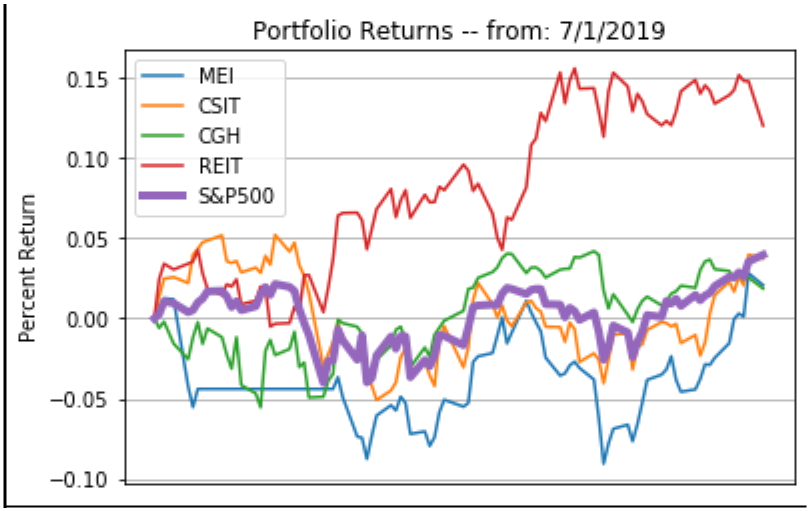
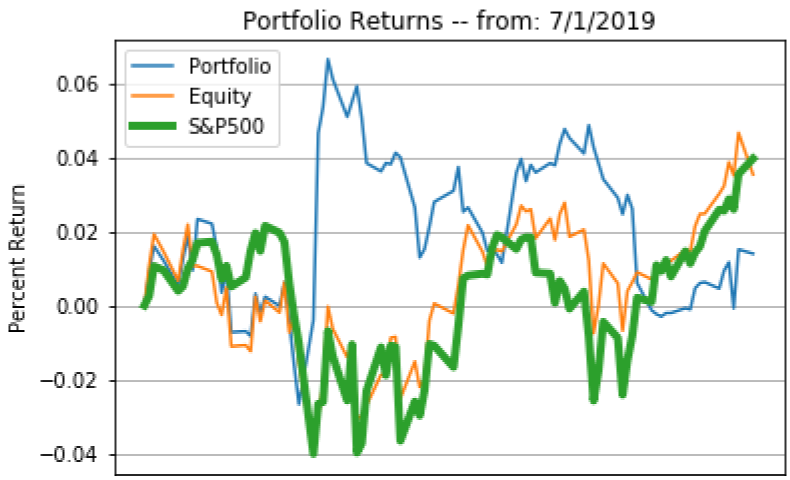
Return Visualizations





Commentary Credits

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