RPM investments
DIFFERENT MOVES.

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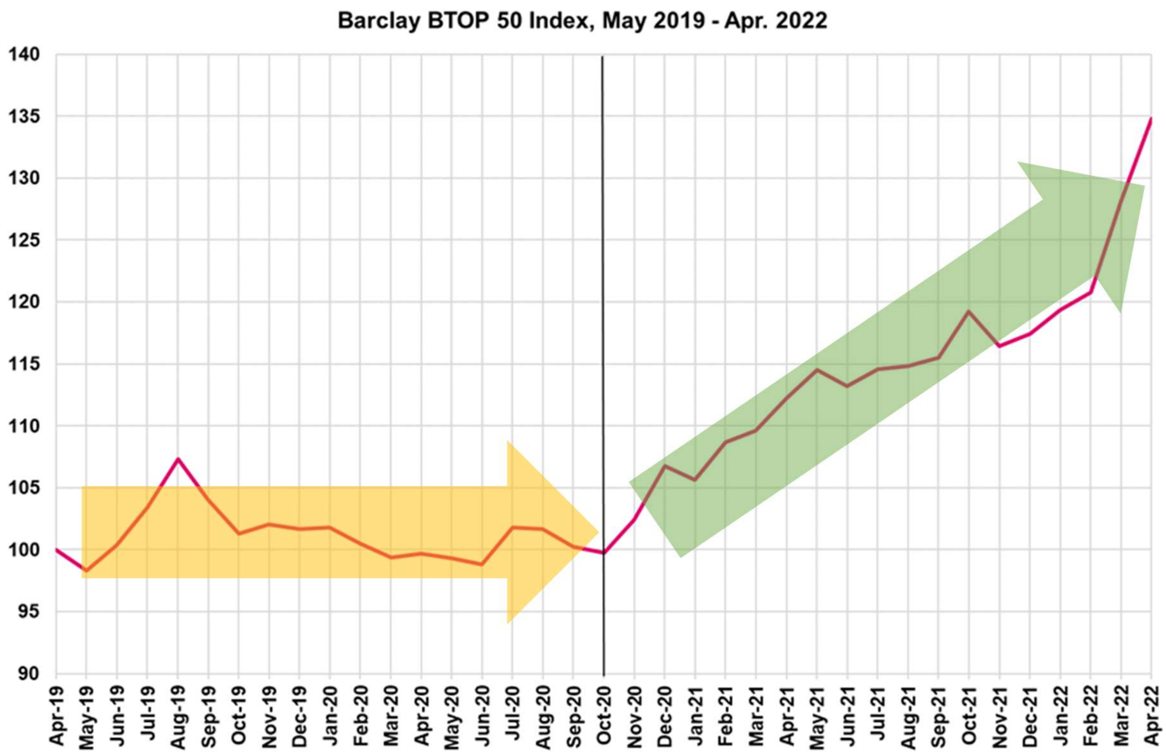
Whoa, what happened?

As of April 2022, CTAs (as measured by the Barclay BTOP50 Index) have returned 35% over the 18 months since the US Presidential Election in November 2020. Over the preceding 18 months, CTAs returned only -0.2%. What happened?



We argue that the shift in performance is the result of price trends caused by evident macro changes. Some of them started already in late spring 2020. CTAs began to perform immediately after the US Presidential Election the same year – about 18 months ago.

The Russian invasion of Ukraine has further strengthened these price trends and CTA performance has continued to be strong.

This Market Commentary concludes with the assertion that financial and commodity markets have entered a new regime, more favorable to CTAs, than the "Central Bank Regime" that has dominated markets since the Great Financial Crisis (GFC) back in 2008.

Looking back

What caused the largely mediocre performance of the CTA industry in the years after the GFC until the autumn of 2020? Several factors were at play:

- ***Negative short-term interest rates*. They were a direct drag on performance (interest is earned on margin and on invested capital) as the famous roll yield turned negative in many markets.**
- ***Political central bank activism*. This activism was visible primarily in equity and bond markets. Market developments that were deemed contrary to political and/or central banks' ambitions often led to interventions, i.e., any sign of equity bear markets or rising interest rates were often met with new support programs with creative acronyms (printing of new money) and supporting rhetoric.**
- ***Synchronized central bank policies* and priorities across developed nations with low growth and low inflation.**

Put together, this created a market environment with generally low volatility and muted price action, which is less favorable to classic systematic CTA trading. Especially bearish trends were often cut short by this interventionism. However, it was tremendously favorable to buy-and-hold strategies in equities and bonds.

Narratives

In our September 2020 Market Commentary, *"A Good Story Drives Markets"*, the main narratives were identified as TINA, FOMA, V-shaped recovery (from Covid-19 crisis), and the Fed backstop.

We suggested that some, or all, of these narratives may soon be replaced by others: "de-globalization", aka "regionalization" as well as "climate change effects". We predicted that this might have a significant impact on price dynamics in both commodity and financial markets.

In *"The Big Picture"* from June 2021, we proposed that a change had indeed occurred. Commodity markets had come to life after a dull decade (energy excluded). We suggested that markets may have entered a new regime – replacing the regime where central bank policy had reigned supreme since the end of the GFC.

A few arguments were listed – basically the same as below. At that time, many of us saw the end of the pandemic and were looking forward to growth and increased prosperity in the world – partly driven by huge investments in new energy infrastructure.

Omicron, inflation, and finally a war in Europe, would put a gradual stop to that optimism.

What changed?

Some of the changes in the world – affecting the CTA industry – that have occurred over the last two years are:

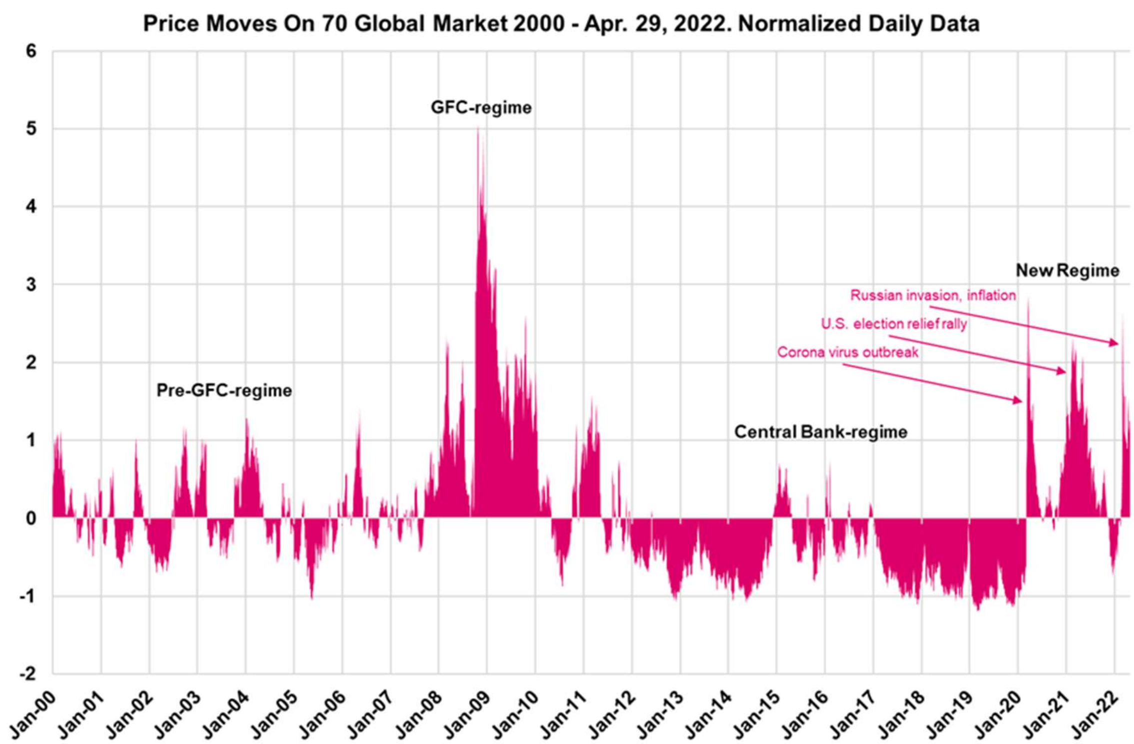
- **Rising inflation, leading to rising interest rates and a turnaround in monetary policy**
- **Global agriculture is increasingly affected by climate change**
- **Governments' pledge to invest in the energy transition**
- **The return of fiscal stimulus**
- **Accelerating de-globalization/regionalization, focus on self-sufficiency**

One effect of these changes is soaring commodity prices: broad commodity indices have more than doubled over the past 24 months.

Another effect is this year's decline in both bond and equity markets.

Short-term factors are adding to this. Post-pandemic pent-up demand, supply chain disturbances, and the Russian invasion in Ukraine.

The result on price action is clear: Market prices are again starting to move in broader ranges. This allows for trends to develop that CTAs can exploit.



The data is calculated by averaging the normalized absolute price moves over 50 timeframes up to one year for 70 different financial and commodity markets.

Current narratives

At the timing of writing, news stories and conversation subjects seem to center around three themes:

- Inflation, possibly even stagflation, and rising interest rates
- The Russian invasion in Ukraine and its effects on markets
- Climate change and the energy transition

Rising interest rates in combination with uncertainty in the equity markets caused both the bond and the equity market to take a combined nosedive in the first quarter of 2022. This is a predicament for the 60/40 investment model that has been the go-to choice for many institutional investors. It has served them well in the previous 10 years, but the future prospects are not very bright.

The themes also support the “Commodity Supercycle” narrative: commodities as an inflation hedge, energy prices skyrocketing due to sanctions, the rise in wheat and other grains prices is accelerated by cuts in Russian and Ukrainian exports and threats of limited exports of fertilizers from Russia and Belarus. Furthermore, a climate related heatwave in India has negative effects on the country’s wheat crops, sanctions on Russia’s energy exports accelerates investments in the green energy transition, etc.

All these arguments point in the direction of continued price trends in many commodity markets.

We would add the de-globalization narrative as a runner-up to the list. With the pandemic still raging in China we have all been made aware of what complicated supply-chains carry in terms of risks for supply shortages and delays. This has had, and will continue to have, a significant influence on prices and price dynamics.

But the dominating theme is perhaps none of these. Instead, a “meta-narrative” of complexity and unpredictability seems to evolve, fueled by the war and the seemingly unpredictable Russian political leadership. World War III? A new cold war? A Russian economic collapse? Nuclear weapons?

People do not enjoy uncertainty, not being reasonably confident of what the near future will look like. To mitigate the discomfort, we either tend to cling to narratives that not only make sense of the present but also stake out the future, or retreat into a wait-and-see, do-nothing stance.

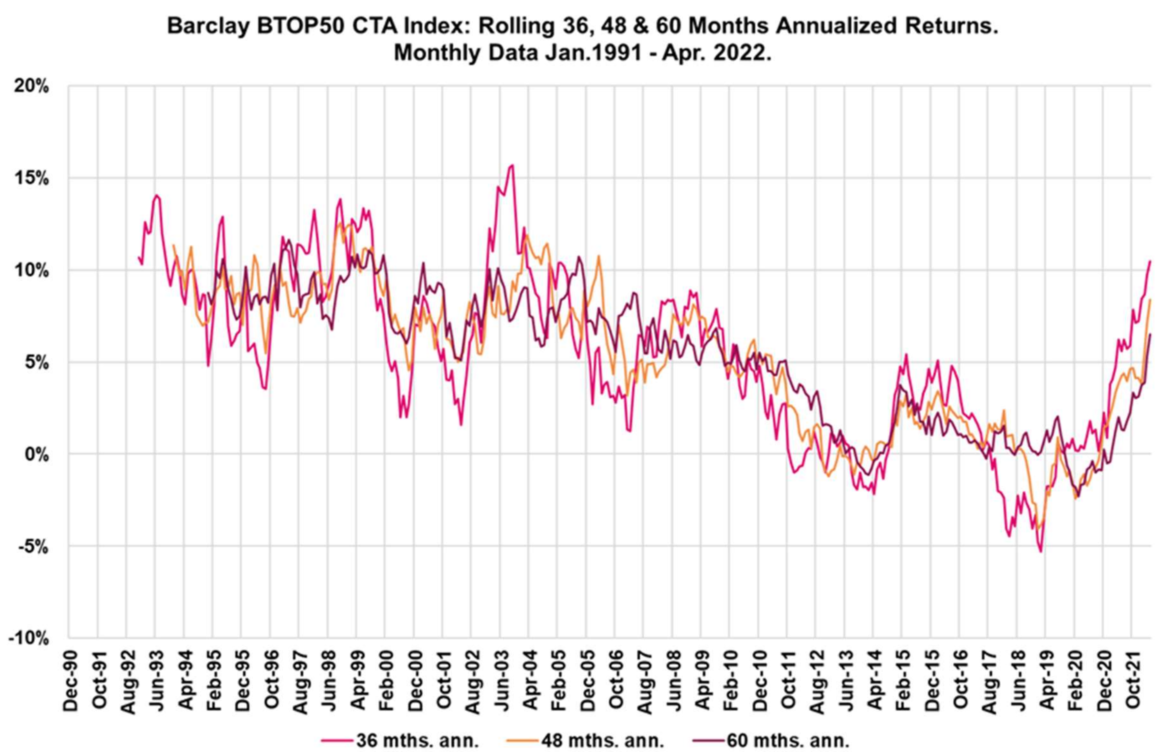
Today, the latter reaction to uncertainty seems to have the upper hand.

The new market regime

Yes, we do believe we have entered the new market regime as suggested already a year ago. Perhaps the most important single factor behind this regime shift is the change in central bank policies: with a no longer “transient” inflation, central banks have started to shrink their balance sheets and raise interest rates.

Climate change, investments designed to mitigate climate change, de-globalization, the shift from monetary to fiscal stimulus, the weaponization of finance, supply chain disturbances and the war in Ukraine are all driving commodity prices which in turn drives inflation. Only the last two of these factors may prove to be temporary. This process started – judging from market behavior – about two years ago.

The new “Post Central Bank Regime” is evident in CTA performance. We must go back 14 years to find longer term performance in line with what we experience today.



Key Takeaways

- **Global markets have entered a new regime characterized by long periods of price trends, driven by macroeconomic, political, and climatological forces.**
- **The future direction of global markets is also perceived as uncertain due to the complexity of the current state of the world.**
- **Markets are moving and volatility is high. The reactive and disciplined trading strategies as applied by CTAs, paired with their ability to go both long and short, make them well-adapted to the current environment and what lies ahead.**

A note on the RPM Evolving CTA Fund

By the end April, RPM's Evolving CTA Fund had returned in excess of 25% so far this year. The fund is the best performing alternative fund on the market-leading investment platform Avanza in Sweden this year and viewed over three years.

Looking forward, we do expect drawdowns to occur. If markets change direction, it will, at least initially, hurt performance. However, the current new market regime tells us that new trends will develop – bull or bear. If so, CTAs will profit from these trends.

For more information, please contact Per Ivarsson, +4684406932, Mikael Stenbom, +4684406910 or by e-mail firstname@rpm.se.

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