

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2019			0.1%	0.3%	4.3%	-4.2%	0.1%	-0.1%	0.9%	-4.1%	7.5%	6.0%	10.5%
2020	-6.2%	-2.0%	2.5%	12.4%	3.6%	-6.6%	19.6%	12.1%	-3.0%	-7.1%	2.1%	11.9%	41.6%
2021	1.1%	3.5%	-0.5%	6.3%	19.5%	-3.2%	4.0%	-5.2%	6.0%	9.9%	-8.1%		35.0%

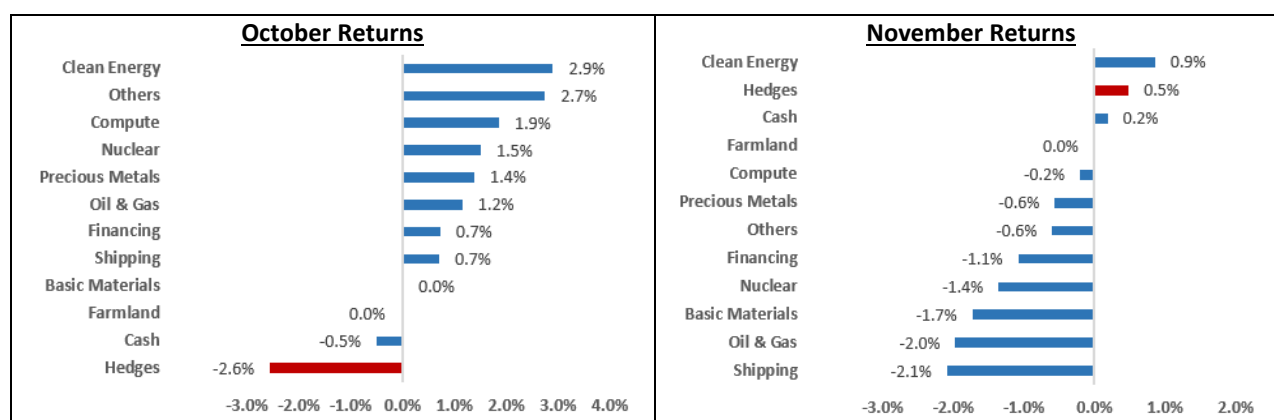
- The Cypress Fund returned 9.9% in October and -8.1% in November. Year-to-date returns are 35.0% net of fees.
- Some of the things we pay attention to warrant concern, including the Fed's hawkish pivot, narrow equity market breadth and price action in high yield bonds, EM FX and crypto.
- Taken together, we urge caution in the short term, ie being judicious in deploying capital and increasing hedge ratios.
- That said, we continue to look for and invest in critically important, real asset-backed businesses. We believe the risk-reward of asset-based investing remains extremely attractive.

Dear fellow investor,

The Cypress Fund returned 9.9% in October and -8.1% in November. Year-to-date, the fund generated net returns of 35.0%.

Investors were bullish across the board in October, driving gains in many asset classes. Notably, Tesla's stock surged over 43% that month, adding over US\$ 340 billion to its market cap and making Elon Musk the richest man in the world. Our fund benefitted from the animal spirits, returning almost 10% with profits in all but one of our investment themes.

November started well, continuing October's trend. Unfortunately, our early gains were erased in the latter half of the month, precipitated by announcement of the latest Covid variant as well as unexpectedly hawkish comments from Fed members. Price action was likely also exacerbated by thin trading volumes post-Thanksgiving in the US. Even with hedges on, our portfolio ended November -8.1%, giving up most of October's gains.




We had written in our [previous investor letter](#) that markets could remain choppy for the time being:

*Financial markets finally cracked in September, after months of deterioration under the surface. The headline reasons for this weakness include China and Evergrande risk, concerns about the US debt ceiling, higher inflation and rising interest rates... we think these are just triggers; **the market's "immunity" has been weakening for a while** making it more susceptible to declines... At this juncture, we still expect the market to chop around; we will update you when our view changes.*

Since we still do not know the severity of latest Covid variant, we suspect that the recent sell-off is a reflection of weak immunity in financial markets. Market participants were looking for excuses to justify reducing risk and Omicron and a newly hawkish Fed fit that bill. While risk assets look oversold in the short term (and hence liable to "bounce"), we would urge caution until such time when we see signs of strengthening "immunity". As many of the measures we track still suggest underlying weakness, our current plan is to play more defensively, acknowledging that we would likely sacrifice some gains should risk-appetites return, yet still preferring this to aggressively buying the dip. In the rest of this letter, we share with you some of the things we are watching that warrant concern.

## I) Fed's Hawkish Pivot

### Yellow: Fed Officials Making Hawkish Comments Recently



FOMC - Hawk/Dove Analysis

InTouch Capital Markets

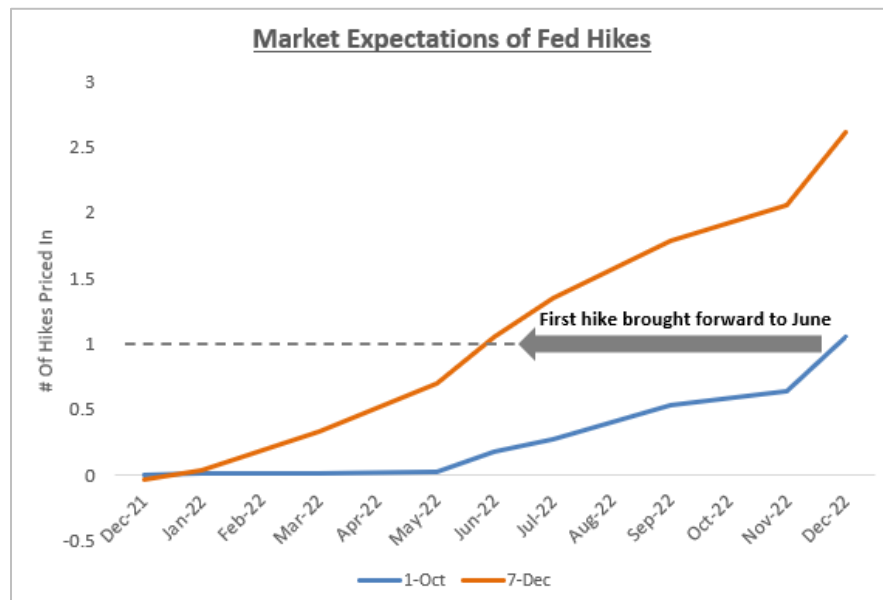
Last Update: 10 November 2021

Name	Position	Hawk Scale	Voter?		
Most Dovish			2021	2022	2023
Kashkari	Minneapolis	<div></div>	✗	✗	✓
Brainard	Board	<div></div>	✓	✓	✓
Evans	Chicago	<div></div>	✓	✗	✓
Daly	San Francisco	<div></div>	✓	✗	✗
Powell	Chairman	<div></div>	✓	✓	✓
Williams	New York	<div></div>	✓	✓	✓
Clarida	Vice Chair	<div></div>	✓	✓	✓
Bowman	Board	<div></div>	✓	✓	✓
Quarles*	Board	<div></div>	✓	✓	✓
Montgomery**	Boston	<div></div>	✗	✗	✗
Barkin	Richmond	<div></div>	✓	✗	✗
Waller	Board	<div></div>	✓	✓	✓
Mester	Cleveland	<div></div>	✗	✓	✗
Bostic	Atlanta	<div></div>	✓	✗	✗
Harker	Philadelphia	<div></div>	✗	✓	✓
George	Kansas City	<div></div>	✗	✓	✗
Black	Dallas	<div></div>	✗	✗	✓
Bullard	St Louis	<div></div>	✗	✓	✗
Most Hawkish					

A number of Fed officials in recent weeks have made surprisingly hawkish comments. Fed Chair Jerome Powell in his 30<sup>th</sup> Nov congressional testimony said that the adjective "transitory" should no longer be used to describe inflation (after insisting on it over the past year) and also hinted at a faster pace of taper.

Lael Brainard, Biden’s nominee for Fed vice Chair and who has consistently leant dovish, also [made remarks](#) about “getting inflation down”. While we try not to over-analyze each and every comment made by Fed officials, there has definitely been a rising chorus warning about higher prices, especially amongst the doves.

We do not know what may be driving this hawkish pivot although we can clearly see from the following chart (extracted from Eurodollar futures) that investors have altered their probabilities of a rate hike, shifting forward the expectations for the first Fed hike to June 2022 from December 2022.



After two years of highly accommodative monetary policy providing a tailwind for investors, such a change could mean more risk aversion from investors.

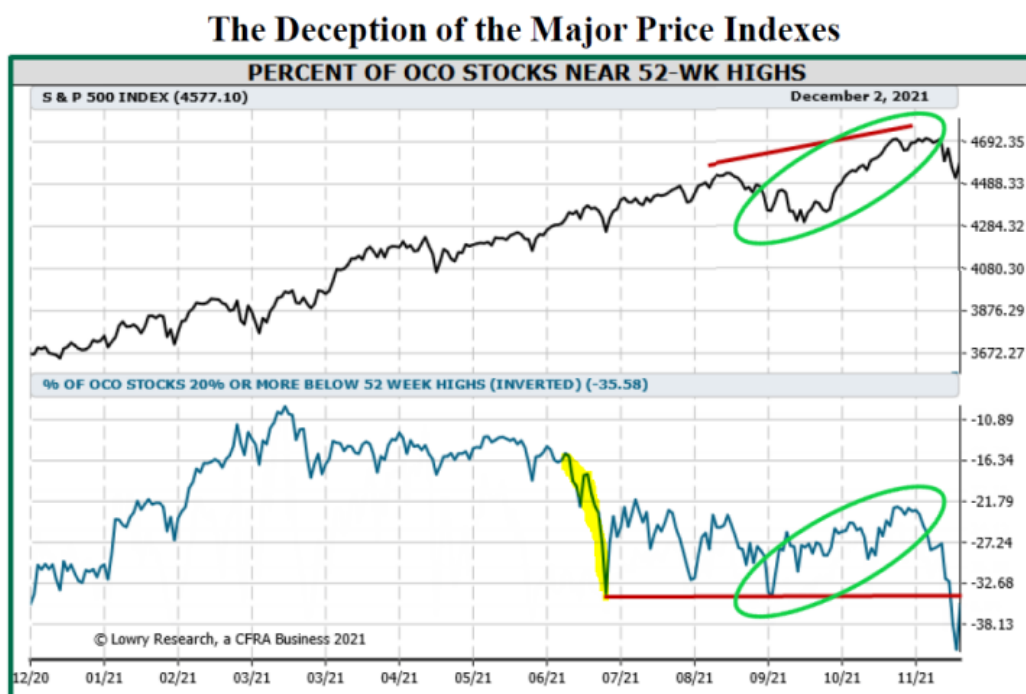
## II) Weak Market Breadth and The Deception of Major Price Indices

In our [2020 year end investor letter](#), we quoted from Lowry Research and their observations about market tops:

*The period leading up to a major market top shares a number of similarities with the Autumn season as it transitions into Winter. That is, in Autumn the leaves begin to fall from the trees in a very gradual process – nearly imperceptibly – one at a time, until the trees are eventually bare at the onset of Winter. It is no different near major market tops. Individual stocks begin to roll over into their own Bear markets, one at a time, usually beginning with the less noticeable small-cap and mid-cap stocks... Thus, as a mature Bull market rallies through a series of higher highs in the big-cap price indexes (such as the DJIA and S&P 500), investors often see that a growing majority of stocks may already be in downtrends. At the final high in the big-cap indexes, a relatively small number of heavily weighted big-cap stocks can deceive investors into believing that the broad market is still in a healthy uptrend.*

In January when we shared these words, we saw few signs of such a topping process in equity markets. This helped shape our view that 2021 could be a good year for risk-taking and we positioned our portfolio accordingly.

The first signs of a transition from autumn to winter appeared in the latter half of June (yellow below), when despite stock indices making new highs, deterioration underneath the surface started to show (% of stocks trading 20% of more below 52-week highs). This was one of the reasons we adopted a more cautious stance in the third quarter of this year, raising our hedge ratios as well as being more selective in our buys. The market correction finally arrived in September, but the quick rebound in October and attendant improvement in the OCO indicator (green ellipses below) suggested that the market could be ripe for risk-taking again.



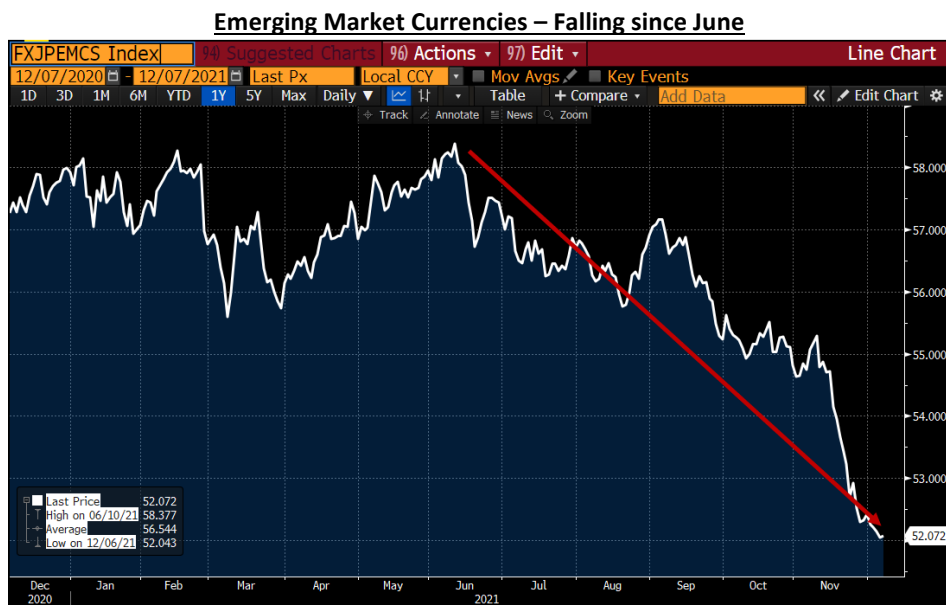
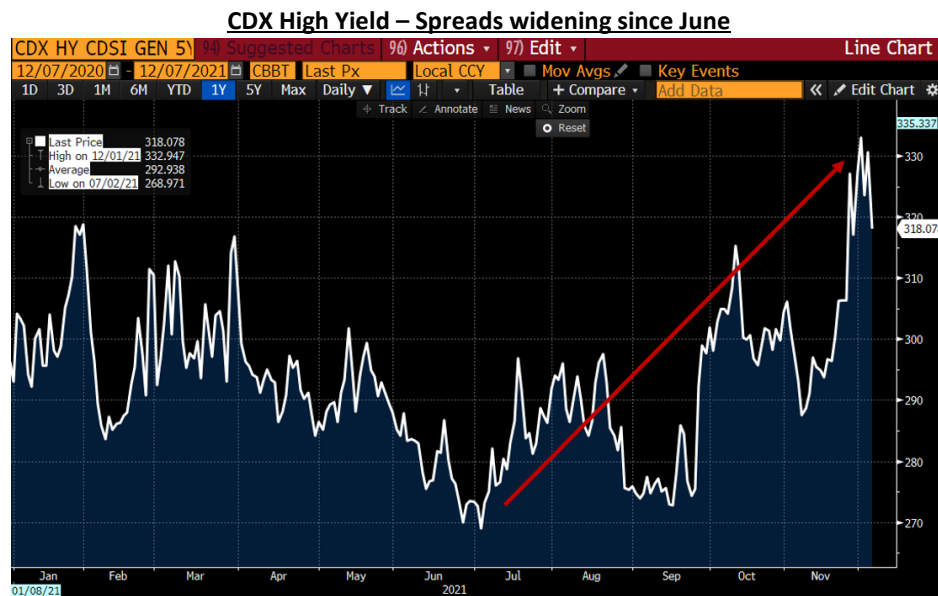
The recent sell-off resulted in the indicator turning sharply lower. Using the S&P 500, even though it is barely 3% from all-time highs (Monday 6<sup>th</sup> Dec), nearly 40% of the underlying stocks are in a “bear market”, ie trading more than 20% from its highs. This is not a healthy sign.

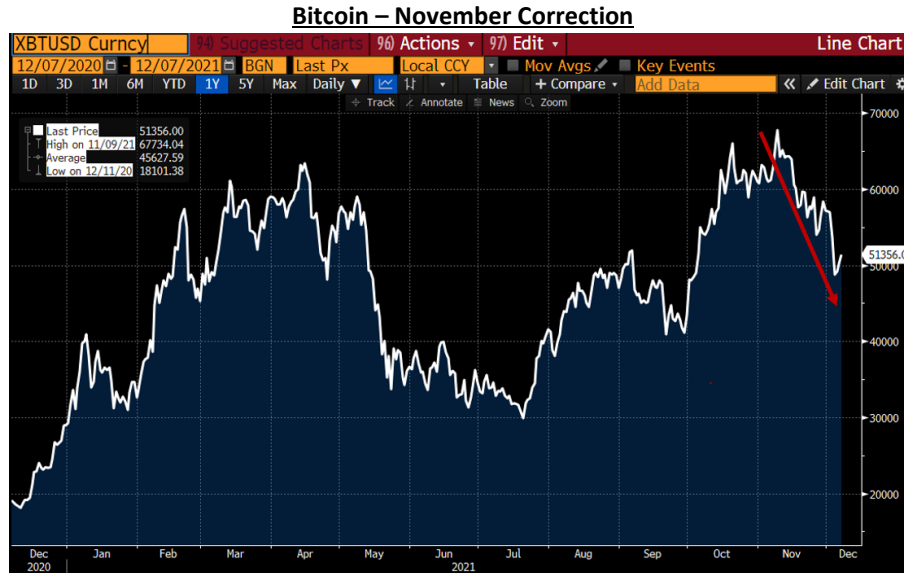
Another way of looking at this is that a very small number of stocks are holding up the performance of market indices. The ARKK ETF stands out in that out of 47 constituents, only five companies are in positive territory for the second half of 2021 and just one stock, Tesla, represents the lion’s share of positive returns.

	Returns (2H 2021)	Contribution (Top 5)	Names
<b>S&amp;P 500</b>	6.9%	4.3%	Apple, Microsoft, Tesla, Nvidia, Google
<b>Nasdaq 100</b>	11.0%	9.4%	Apple, Microsoft, Tesla, Nvidia, Google
<b>ARKK</b>	-26.3%	5.9%	Tesla, Unity, Coinbase, Sea, Cerus

### III) Risk-Off in High Yield Bonds, Crypto and FX

Other risk asset classes are also in risk-off mode. High yield CDX spreads have been widening since the middle of the year, as have emerging market currencies, another gauge of risk sentiment. More recently, bitcoin and other crypto currencies have also been selling off. In our view, more important than the possible reasons for such price action is the fact that these markets are all telegraphing investor risk aversion; in the cases of high yield and FX for many months already. We may not understand the reason why animals have sometimes been observed to flee before natural disasters, but it pays to heed their warning.





### Conclusion – Stay the Course but be Prepared for Volatility

After the previous sections, readers may conclude that one should go to cash given the warning signs we highlighted. We do not believe we are at that point yet.

From a fundamental perspective, the companies we own continue to benefit from structural supply-demand dynamics, irresponsible monetary policies and attractive valuations. We still stand to make very substantial profits as investors re-allocate to real assets (see appendix).

While we believe this will be the case over the coming years, there will also be times when grey clouds appear and the sea turns choppy. We have been seeing them since the middle of the year and there are still no obvious signs that they are abating. Given this, we do believe that we need to strap ourselves in and be prepared for more volatility. We are not changing course, just bracing for rough waters.

I hope this short note has been helpful and do reach out with your questions or comments. Till we connect again, thank you. Wishing you and your loved ones a joyful end to 2021 and a blessed Christmas.

Sincerely,

Yongchuan Pan  
8 December 2021

Theme	Thesis	Upside	Risks
Nuclear/Uranium	<ul style="list-style-type: none"> <li>• Growing acceptance of nuclear as source of carbon-free energy</li> <li>• Growing demand and falling supply for uranium</li> <li>• Priced below marginal cost of production</li> </ul>	100-300%	<ul style="list-style-type: none"> <li>• Larger amounts of secondary inventory than expected</li> <li>• Another Fukushima</li> </ul>
Shipping	<ul style="list-style-type: none"> <li>• Extremely favourable supply dynamics for tankers and LPG vessels (old fleet, few new build orders)</li> <li>• Stocks trade at discounts to NAVs with large dividends (&gt;10%)</li> </ul>	100-200%	<ul style="list-style-type: none"> <li>• OPEC+ production cuts</li> <li>• Recession</li> </ul>
Basic Materials	<ul style="list-style-type: none"> <li>• Adriatic Metals trading at substantial discount to NPV</li> <li>• Heavy insider ownership with likely takeout by current shareholder</li> <li>• Leverage to silver price without paying for it</li> </ul>	100-300%	<ul style="list-style-type: none"> <li>• Country risk</li> <li>• Construction risk</li> <li>• Lassonde curve</li> </ul>
Computing Power	<ul style="list-style-type: none"> <li>• Surging chip and tin consumption due to increasing demand for compute – automobiles, IoT, defence</li> <li>• Demand not priced in at all at current multiples; huge exploration upside for free</li> </ul>	50-200%	<ul style="list-style-type: none"> <li>• Recession</li> <li>• Idiosyncratic company risks</li> </ul>
Precious Metals	<ul style="list-style-type: none"> <li>• Protection against inflation and fiat debasement</li> <li>• Under-owned by official sector/central banks</li> <li>• Potential alternative to bonds – producers trade at high and growing free cashflow yields</li> </ul>	100-500%	<ul style="list-style-type: none"> <li>• Strong economy with low inflation</li> <li>• Regulatory risk</li> <li>• Challenge from crypto</li> </ul>
Clean Energy Transition	<ul style="list-style-type: none"> <li>• Climate change is driving energy transition; this shift to cleaner energy will rely heavily on electrification</li> <li>• Own highest quality copper producers levered to higher prices with exploration upside</li> </ul>	100-400%	<ul style="list-style-type: none"> <li>• Recession</li> <li>• Idiosyncratic company risks</li> </ul>
Oil & Gas	<ul style="list-style-type: none"> <li>• Energy transition will take longer than expected; fossil fuel use will remain for decades to come</li> <li>• Own producers and offshore service providers pricing in much lower crude oil and natural gas prices than in the market</li> </ul>	100-400%	<ul style="list-style-type: none"> <li>• Recession</li> <li>• Regulatory risk</li> </ul>
Farmland	<ul style="list-style-type: none"> <li>• Growing demand for food and improving productivity driving higher yield for farmland and hence valuations</li> <li>• Overlooked asset class, 20-30% discounts to fair value, dividend-paying</li> </ul>	50-100%	<ul style="list-style-type: none"> <li>• Recession</li> <li>• Poor harvests / climate anomalies</li> </ul>
Financing	<ul style="list-style-type: none"> <li>• Own equity in structured financing vehicles</li> <li>• Substantial upside with very limited risk</li> </ul>	50-100%	<ul style="list-style-type: none"> <li>• Opaque and hard to analyze</li> <li>• Narrative too complicated for most investors</li> </ul>