Technology of the Future Fund

We find the leaders of the future

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MONTHLY REPORT

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Executive Summary

- The Omicron Coronavirus variant was the biggest theme in markets in December and led to a significant sell-off in early January.
- **In our view this latest COVID wave will result in a pick-up of vaccination rates and can accelerate the end game for the pandemic – as more exposure, more vaccines, and effective treatment will move us towards endemicity faster.**
- The bond market responded to the hawkish Fed minutes that added fire to the equity sell-off. Interest rates rose sharply with the 10-year Treasury yield going from 1.40% to 1.76%... above the 2021 peak. The next level is 2.0%.
- **Fed funds futures now price in an 86% chance of a March 2022 rate hike.**
- Technology stocks have been the main victims of higher interest rates expectations. In 2021, **40% of Nasdaq member companies fell by more than 50% from their 52- week highs**. Technology growth stocks do not perform well when interest rates rise.
- **We offer investors a contrarian view on technology stocks. While we think in 2022 – 2023 technology stocks will continue to underperform, this will be the best time to accumulate strategic positions (on the way down) in these companies, which will be the leaders in the current business cycle and will outperform the major equity indexes on a 5-10-year time horizon.**
- The Technology of the Future Fund had a -4.71% return in December, underperforming the benchmark MSCI World Index (USD), which had a return of +4.19%.

Economy and Markets

Many 2022 strategy views were thrown in the bin in the 1st week of January, as the COVID numbers were absolutely incredible and far beyond even the most aggressive forecast. The Omicron variant has led to some profit-taking in segments where valuations were excessive.

Omicron has confirmed our main thesis re Coronavirus, which we passed to our clients in Nov 2020: “The COVID virus behaves similarly to influenza, and we will have to learn to live with it. It will mutate, disappear, and reappear. A COVID-19, “2.0”, 2021 mutation might require a different vaccine. But with each modification, the virus will become weaker and less severe.”

Our base case is unchanged since November 2020: New COVID waves will continue to resurface but each wave will be less severe and will bring humanity closer to the “herd immunity” state.

Another key theme in the markets was the Fed’s more hawkish tone, with Chair Powell speeding up the tapering process. This resulted in increase in volatility in December and early January. Minutes from the December FOMC revealed that starting Quantitative Tightening (QT) closer to liftoff of taper and proceeding at a faster pace than the last cycle was indeed the position of the Committee. This added fire to the equities sell-off. Fed Funds futures now price in an 86% chance of a March 2022 rate hike, up from 63% at the close on New Year’s Eve, just 27% at the end of November and 0% in early October. Some economists also believe that QT will commence after two rate hikes, starting sometime in the third quarter.

Investment Strategy and Portfolio Changes

2021 like 2020 (pandemic year) was a stimulating year for our team when our strategy was again tested in a difficult environment. In both years we were able to control the drawdown of the portfolio as we did not own any overpriced growth stocks. In addition, our risk management process which is based on price discipline and strict risk management procedures worked well in both years. In 2021 the Technology of the Future Fund delivered -9.86% return, while the max drawdown was -14.80%. 2021 was a difficult year as a "once in a decade" shift in monetary policy of major central banks negatively impacted technology innovative stocks. In the course of 2H 2021 we continued to focus on alpha generation for the long term and less on market directionality. We were buying assets – increasing our core positions as the prices were going down.

It is our understanding that the Nasdaq index delivered +22% return because the investors were hiding in a small number of the biggest mega cap tech stocks and ETFs loaded with them. Given that market concentration is so high, a small part of the market is increasingly responsible for huge gains. At the same time 40% of Nasdaq member companies fell by more than 50% from their 52-week highs (source: Bloomberg story).

We expect a challenging time for our portfolio in 2022 – 2023 as technology growth stocks do not perform well when interest rates rise. Current macro conditions suggest that US 10Y bond yield should be rising (it was above 3% in 2018), lifting the discount rates, which have been unusually low since 2020. The rise in US bond yields is likely to put an upward pressure on the discount rate, used in the calculation of the fair value of companies, as the risk-free-rate (RFR) rises. As a result, the valuation of growth technology stocks will decrease in coming years.

For example, one of our top picks in the cloud analytics/Big Data segment, Snowflake, is one of the most sensitive stocks to higher discount rates. We sold the fund's position in summer 2021 as the valuation was demanding (x 50 2021 P/Sales multiple). Based on quantitative data, provided by Jefferies, a 50 BP increase in RFR from 1.5% to 2.0% can result in an average P/E ratio of 220 rerating to a P/E of 40 in the course of few years. Snowflake is already down 25% since its peak in November 2021. We are looking forward to buying back our position in Snowflake at a lower level, as the company is a strategic beneficiary of the continuation as we see it of cloud data analytics as a cornerstone of corporate digital transformation.

At the same time small innovative companies will experience difficulty in raising capital in a period of high volatility and falling markets.

We offer investors a contrarian view on technology stocks. While we think in 2022 – 2023 technology stocks will continue to underperform, this will be a good entry point in carefully selected strategic positions (on the way down) in the companies which offer robust long-term opportunities and which will be the leaders in the current business cycle and outperform the major equity indexes on a 5-10-year time horizon.

Adding an investment strategy which is uncorrelated to an overall multi-asset portfolio reduces the overall riskiness of the portfolio. And allocating capital to an aggressive asset class via risk-controlling managers has been a very profitable way of investing in the past.

Overall, we recommend that investors reduce their equity exposure by the end of 2022, as we expect some tactical weakening of equity momentum, but maintain an investment in our fund as a source of risk diversification and exposure to a strategy which has low correlation with major equity indexes. The majority of the stocks in our portfolio are absolute return investment ideas, which generate significant alpha and deliver outperformance in the portfolio regardless of what is happening in the general market or economy.

In December we sold our position in Chinese car manufacturer **Geely**, as we saw better risk reward in Chinese electric car producer **Nio**, where we have opened a new position. We have opened a position in one of the best Chinese biotech companies **Wuxi Biologics**.

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Monthly performance %

As of 31.12.2021

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2020	-0.11%	+0.79%	-7.86%	+6.45%	+8.51%	+6.03%	-0.17%	+1.51%	-0.22%	-1.39%	+18.08%	+3.22%	+38.07%
2021	+2.05%	+0.35%	-3.43%	+3.61%	-0.57%	+3.70%	-4.32%	-2.38%	-4.22%	+5.11%	-4.91%	-4.71%	-9.86%

Performance since inception (Aug 2019): +26.50% vs MSCI World (USD): +47.73%

Technology of the Future Fund performance vs. major equity indexes

	December 2021	YTD 2021
Technology of the Future Fund (USD)	-4.71%	-9.86%
S&P 500 (USD)	+4.36%	+26.89%
NASDAQ 100 (USD)	+1.14%	+26.63%
NASDAQ Biotech (USD)	-1.31%	-0.63%
DJ Stoxx 600 (USD)	+5.66%	+13.79%
MSCI EM (USD)	+2.11%	-4.12%
Shanghai Composite (USD)	+2.32%	+7.65%
MSCI World (USD) (Fund's benchmark)	+4.19%	+20.14%

Performance contributors

December 2021

Top contributors	Return %	Contribution
Zogenix	+44.44%	+2.36
Invisio	+5.13%	+0.29
Western Digital	+12.74%	+0.27

Bottom contributors	Return %	Contribution
Arqit Quantum	-37.07%	-1.65
Daqo New Energy	-29.68%	-0.70
Renewable Energy	-11.18%	-0.50

Performance Contributors, December 2021

The shares of US biotech company Zogenix (+44.44%) went up as the company continued successful execution and business development, as well as submitting a New Drug Application for key drug FINTEPLA® (Fenfluramine) in Japan for the Treatment of Epileptic Seizures Associated with Dravet Syndrome. Also, the company has submitted a Type II variation application to the European Medicines Agency (EMA) to Expand the Use of FINTEPLA (Fenfluramine) for the Treatment of Seizures Associated with Lennox-Gastaut Syndrome. The company's performance is a good example of biotech stocks performing under any market scenario when there is good news regarding key drugs. Market volatility was the only reason for the bounce back of the shares of Swedish communication company Invisio (+5.13%). The shares of the US maker of hard drives for businesses and personal computers Western Digital (+12.74%) went up as the company reported a 283% surge in earnings on a 29% hike in sales in 3Q. Western Digital makes solid state and hard disk drives for personal computers and enterprise computer systems. Semiconductors have been in short supply, including solid state flash memory chips like those WD makes. As chipmakers ramp up production, computer makers also need the hard drives Western Digital makes. The shares of UK cyber security company Arqit Quantum (-37.07%), which offers quantum encryption technology, corrected after stellar performance in November 2021 (+74%). We have bought back half of our position, which was sold at November highs. The shares of Chinese polysilicon manufacturer Daqo New Energy (-29.68%) went down as investors anticipated a retreat in polysilicon prices in the coming quarters. We maintained our position without any changes as we consider Daqo New Energy as a key beneficiary of climate change and solar power achieving grid parity across the globe through cost reductions. The shares of US biodiesel producer Renewable Energy (-11.18%) went down based on market volatility.

Portfolio Structure

Our defensive positioning and high cash level in 2H 2021 based on the expectation of increased interest rates and meaningful correction in equity markets in 2022 was fully justified. December 2021 and the 1st week of January brought a lot of investment opportunities. For the first time since the launch of the fund (August 2019) we have spent almost all our cash without looking at the market directionality, as many of our strategic holdings have fallen to very attractive risk/reward levels. We think the markets are only at the beginning of high turbulence, which is expected in the course of 2022. But we managed to add to our strategic holdings at very attractive prices, and this will result in outperformance in the long run. In 2022 we expect many positive surprises from our biotech holdings (22% of the fund) and we think our Chinese tech holdings are ready for a mean reversal.

Top 5 holdings

Company	Portfolio weight
Axon	**6.2%**
Baidu	**5.7%**
Invisio	**5.7%**
Zogenix	**5.3%**
Meituan	**4.9%**

Portfolio structure