



Quarterly Letter June 2015

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THALASSA CAPITAL LLC

“You never want a serious crisis to go to waste.” Emanuel Rahm

As we begin to write our Investors’ Quarterly Letter, the never ending Greek drama takes a new turn injecting additional volatility in global markets.

A renewed “Lehman Moment” would not seem in the cards as the contagion risk of this crisis is constrained by multiple elements such as the European Central Bank holding most of Greek sovereign debt (as opposed to private investors in the 2008 crisis), the small size of the Greek economy and the slow motion unfolding of these events. Interestingly, the Euro, probably one the most vulnerable instruments in the case of a Grexit, is actually up on the day (Monday 29th) after recovering deep overnight losses.

Whether the European political elite will not let this crisis go to waste, as Mr. Rahm famously stated a few years ago in regards to the 2008 mayhem, we should know in the next few weeks.

From our perspective, the risk of contagion and the political response are important factors to monitor as we fine tune our strategy and allocation for the second part of the year.

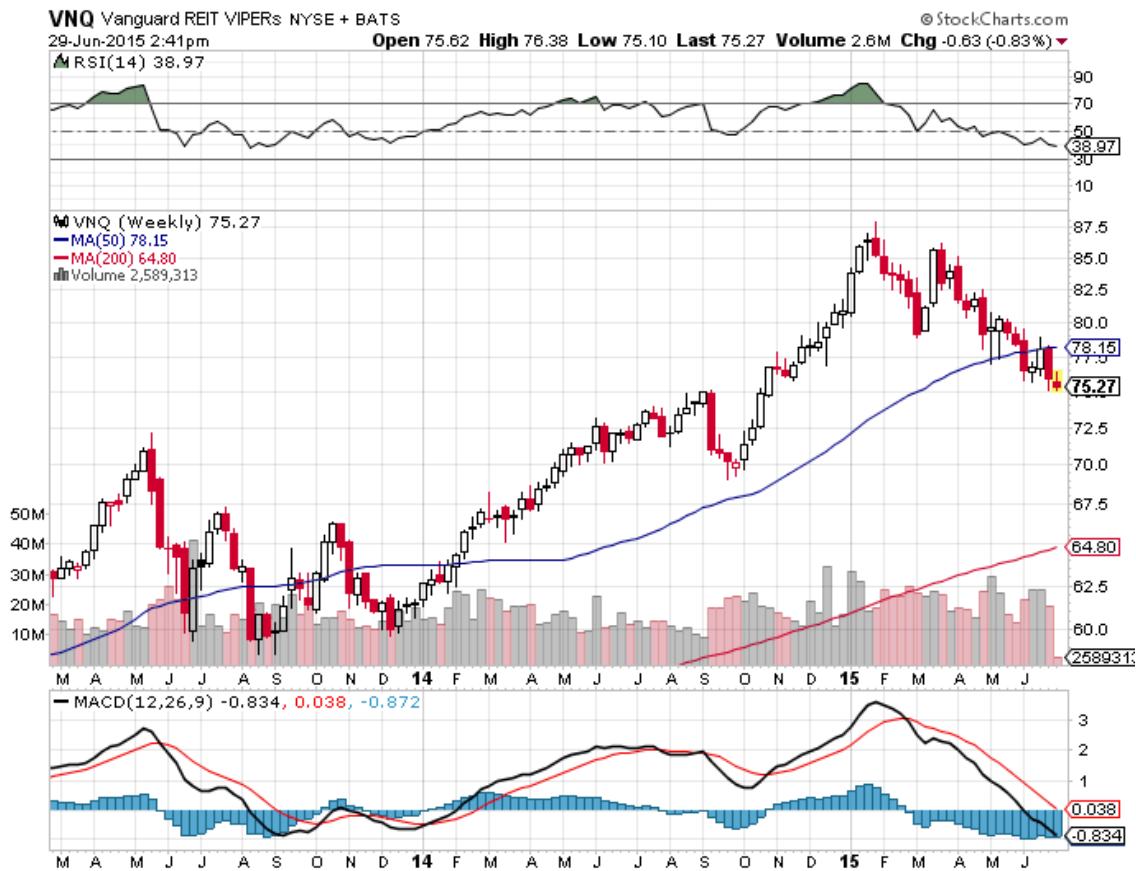
A prolonged and increased volatile management of the Greek crisis would seem to put the brakes on interest increases here on the United States creating a positive counter-balancing effect for equities and income products. Equities are currently priced at fair value or slightly above historical averages and therefore selectivity is key in adding exposure at this juncture.

One problem with current valuations and future expected rates of return is the aggressive trend in corporate buy backs. A significant portion of expanding multiples is due to corporations buying back their stock (and often getting engaged in merger activity as well); on a short term basis we can see the benefits but this is dry power that is being taken away from the markets in the future. This also may affect Capex allocations and push inflation higher at a faster rate.

The key themes we have identified in the last two missives remain in vogue: alpha over beta and selectivity in energy and energy infrastructures. This may sound repetitive but we believe that patience is key as we wait for new opportunities to develop.

Patience is certainly key as we place bets in energy. As the supply imbalance gets worked out, we eventually expect rising oil and NGL prices along with lower extraction costs. However, the short term contingency may continue to put pressure on the sector as we still see low cost inventory coming to the market such as cheap production in the Marcellus area.

Another sector that may be getting ready to provide opportunities is the REIT market. REITs have corrected significantly since their January top and are back on our radar screen as we indicated in our blog dated June 15th. The uncertainty over future monetary policy still keeps the sector under pressure but by the time the first hike comes we may start to see attractive sector values.



Source: www.stocharts.com

Another potential upcoming opportunity could be in Emerging Markets. These markets have underperformed the US and developed economies in the last five years and may be due for a reversal of fortune on technicals alone. A systematic country model run by JP Morgan also puts the spotlight on Emerging Markets favoring them over Euro and UK area economies. The model screens countries by three parameters: price-to-cash flows, changes



in exchange rates and changes in manufacturing PMIs. The short term problem with EM is still the future path of monetary policy in the US; however, on a longer time frame they do seem to provide value.

In conclusion, in our view the biggest threat to a positive second half of the year is not any volatility associated with Greece but rather monetary policy normalization within a context of anemic growth and possibly accelerating inflation.

We will be monitoring central bank action in conjuncture with macro data and we will attempt to separate the noise from the fundamentals.

As always, we would like to thank you for the renewed confidence in our work,

Youri Bujko

Davide Accomazzo