

# Market Guide

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“Wise spending is part of wise investing. And it’s never too late to start.”

- Rhonda Katz

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## Short Selling: A New Tool for Investors

The aggressive monetary tightening being pursued by many central banks to stem historically high inflation and the risk of a slowdown in the economy has pushed many stock markets into bear territory. Bear markets often present opportunities for investors to profit through short selling, a product that will soon be introduced on the Jamaica Stock Market. Year to date, amid the 19% drop in the S&P 500, US short sellers have made US\$405Bn betting against the market, earning mark-to-market<sup>1</sup> profits in all but one sector: gravity-defying energy<sup>2</sup>.

### What exactly is short-selling you may ask?

Short selling is a type of investment or trading strategy that speculates on the decline of a stock or other security's price. It involves an investor borrowing a security from a broker-dealer to sell on the open market, with the intention of buying it back at a later time at a lower price than it was initially sold at. Investors and traders typically make the assumption that the price of a stock will decline based on expectations that market fundamentals will worsen, the presence of a bear market or prediction of a pending bearish trend around a stock based on technical indicators, valuations reaching elevated levels, or any other factor that can affect a company's earnings or stock price.

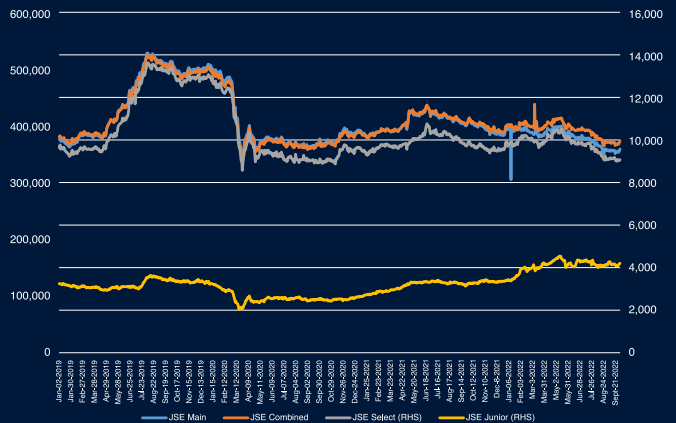
### Why short sell?

This type of investment strategy is typically used for speculation by traders, and investors or portfolio managers to hedge against the decline of securities in their portfolios. Using short selling for speculation, which is focused on making a quick profit by taking advantage of price fluctuations, carries the potential possibility of substantial risk, while hedging is a more common transaction to offset positions, thus reducing risk exposure. For example, this would come in handy in the current environment where prices are falling off due to the rising interest rate environment. Portfolio managers could use shorting as a hedge to mitigate losses or achieve gains by taking a short position in stocks that were previously purchased for the portfolio.

### How does shorting work?

As mentioned above, investors borrow a security whose price they think is going to fall from their brokerage and sell it on the open market. The intention is to buy back the same stock later, hopefully for a lower price to make a profit. In order to short sell, a margin account must be established to hold the securities that are being borrowed. An investor's margin account<sup>3</sup> contains securities bought with a combination of the investor's own money (used as collateral), and

### WEEKLY MOVEMENT IN INDICES



### MOVEMENT IN INDICES

JSE Indices	Closing Levels	WoW % Change	YTD % Change
Combined Index	362,901.35	-1.29%	-9.5%
Main Market Index	348,203.83	-1.48%	-12.1%
Select Index	8,831.65	-1.71%	-10.6%
Junior Market Index	4,150.00	0.40%	+21.1%

### WINNERS & LOSERS (FOR THE WEEK ENDED OCT 31, 2022)

	\$ Change	% Change
Eppley Limited 5% Pref Share	+\$5.28	+29.1%
TTECH Limited	+\$0.59	+21.9%
MPCCEL	-\$0.34	-35.9%
PAL	-\$110.93	-13.4%

### MARKET OVERVIEW

For the second consecutive week, most major indices declined, save for the Junior Market index which appreciated by 0.4%. Appreciations in the prices of Knutsford Express Limited (KEX) and MFS Capital Partners (MFS) Limited supported the increase in the Junior Market Index. After turning around its pandemic related losses into a net profit for its financial year ended May 2022, KEX continued the recovery in its profitability in Q1 of its new financial year with earnings of \$84.23 Mn relative to \$9.20Mn in the prior period. The upward trend in profitability for KEX was largely attributed to the full reopening of the economy as well as increased tourism arrivals, which increased demand for its services. Consequently, investor sentiment around the stock improved. Meanwhile, since the MFS takeover of SSL Venture Capital the stock price has been appreciating, likely due to increased optimism around future business developments.

Overall 127 stocks traded last week of which 47 advanced, 65 declined and 15 traded firm. The main advancer was Eppley Limited 5% preference shares which increased by 29.14%. However, it should be noted that the volumes traded for this stock were thin. The other main advancers were the previously mentioned KEX and MFS, as well as TTECH limited. TTECH limited has been on a declining trend since the start of the year. The appreciation last week was the stock regaining some value from the previous week when it was trading at one of its lowest price level year-to-date. Notably, the stock also trades on thin volumes which would have contributed to its stock price appreciation.

1. Marking to market refers to the daily settling of gains and losses due to changes in the market value of the security.

2. S3 Partners Research

money borrowed from the broker. Therefore, once the stock is sold, repurchased at the lower price, and the stock returned to the broker, the investor would then pocket the difference after repaying the initial loan.

Take the following for example: Transjamaica Highway (TJH) shares, which are listed on the JSE, have declined by 13.3% year to date, but rose to a high of \$1.76 in April. Let's say a trader borrowed 10,000 shares from a broker, when TJH was trading at \$1.76 on April 8th and sold them to another investor. The trader is now "short" 10,000 shares, since he did not technically own the shares, but borrowed them. On October 28th, the share price dropped to \$1.36 and the trader decided to close the short position. He buys 10,000 shares at \$1.36 to replace the shares borrowed and returns them to the broker. The gross profit on the short sale (excluding commissions and interest on the margin account) is \$4,000.00 ( $\$1.76 - \$1.36 = \$0.40 \times 10,000 \text{ shares} = \$4,000.00$ ) or 29.4%.

### Pros and Cons of Short Selling

Short selling plays an important role in efficient capital markets, conferring positive benefits by facilitating secondary market efficiency and trading of securities through improved price discovery<sup>4</sup> and liquidity, while also positively impacting corporate governance which ultimately benefits the real economy. The Jamaica Stock Exchange plans to implement this type of trading strategy, which should drive more stock market activity and provide investor versatility, without making the wider market vulnerable to collapse. Furthermore, trading on margin gives leverage to investors, meaning that little initial capital is required. Additionally, if successfully executed, short selling can be an inexpensive way

to hedge and provide a counter balance to other holdings in a portfolio.

However, it is an advanced type of strategy that is recommended to only experienced traders and investors because of the risks. While you have the potential to earn big profits, you may also make unlimited losses. An investor who has shorted a stock can make unlimited losses in a short since there is no ceiling for a stock's price. For example, in the TJH example above, if the stock price had risen instead of falling, the trader could lose infinite amounts as there is no limit to which a stock can increase. Additionally, a short-seller may have trouble finding enough shares to buy when it comes time to close out a position if there are many other traders also shorting the same stock, which could result in the him losing the profit-making opportunity. Sellers may also get caught in a short squeeze<sup>5</sup> loop if the market, or a particular stock, starts to climb rapidly. For example, this was observed with GameStop in 2021 where short sellers were forced to buy back the stock and cover their positions to limit their risk, when the stock caught the attention of retail investors through social media and significant demand for the stock was generated sending the price of the stock higher.

Short selling will prove to be a useful tool to investors to increase the variety of investment strategies available to them to mitigate risks and generate rewards, while simultaneously improving market efficiency. No longer will investors be limited to the buy low- sell high strategy, which is considered to be investing basics. Now, there are greater chances to increase returns and hedge buy positions, adding balance to the market. There will also be better price discovery limiting overvaluation of

**Short selling plays an important role in efficient capital markets, conferring positive benefits by facilitating secondary market efficiency and trading of securities through improved price discovery and liquidity.**

stock prices. While these benefits are attractive, with great reward comes risks that investors must be mindful of when employing short-selling strategies.

3. Margin Account - A margin account is created by a broker for a customer—essentially lending the customer cash to buy securities. The margin requirements essentially act as a form of collateral, or security, which backs the position and reasonably ensures the shares will be returned in the future.

4. Price Discovery - The process of finding out the price of a given asset or commodity.

5. Short Squeeze - A rapid increase in the price of a stock owing primarily to an excess of short selling of a stock rather than underlying fundamentals.

## Foreign Exchange Market

The Jamaican dollar depreciated by 0.18% relative to the USD last week, with the USD selling rate moving from J\$153.82 on October 21st, 2022, to J\$154.09 on October 28th 2022. The depreciation was fuelled by tight liquidity in the US market coupled with high demand.

Selling	Close: 21/10/22	Close: 28/10/22	Change
J\$/US\$1	\$153.82	\$154.09	+\$0.27
J\$/CDN\$1	\$112.88	\$113.92	+\$1.04
J\$/GBP£1	\$173.30	\$178.16	+\$4.86

## Global Bond Prices

Global Bond prices rallied over the week as inflation numbers declined and talks of a 'policy-pivot' permeated the market. Assertions were made by Wall Street that the Fed will debate how to communicate a smaller rate-hike step in December, after the 75-basis point rate hike anticipated for this week (Nov.2). This was the primary catalyst for last week's rally effort. The market is looking forward to language that supports a pivot to a less aggressive path going forward and has priced this in.

Furthermore, there were no quantifiable recession conditions in the US in the third quarter. Real GDP increased at an annual rate of 2.6%. The key takeaway from the report is that it ends a two-quarter streak of negative GDP prints. It also suggests the economy held up well in the third quarter as it started to acclimate to rising interest rates.

This rally in prices would have resulted in the 10-year treasury yield decreasing from 4.21% to 4.01% week over week as investor demand increased, which placed downward pressure on yields.

Bonds	Current Rating	Indicative Price	Yield	Recommendation
Sagior Fin 2028 (5.30%)	BB-/ Positive	94.23	6.56%	BUY
TPHLTT 2029 (9.00%)	BB/ Stable	107.00	7.65%	BUY
MARFRIG 2026 (7.00%)	Ba2/ Positive	99.00	7.33%	BUY
BERMUD 2027 (3.72%)	A+/ Stable	98.00	4.24%	BUY

## GOJ Globals

Ticker	Maturity	Bid	Offer Yield*
JAMAN	2028	108.00	5.06%
	2039	114.25	6.57%
	2045	110.25	6.97%

\*NB: The rates quoted above are opening indicative levels on the international market and are subject

to change as market conditions vary throughout the trading session. Additionally, the prices quoted to clients of NCB Capital Market Limited (NCBCML) are adjusted to reflect the costs associated with completing the transaction on the respective client's behalf.

## Local Corporate Bonds

Name	Maturity	Coupon	Price	Yield
GHL	2026	6.75%	105.00	6.47%
JBG	2028	6.75%	104.20	5.95%
Seprod	2024	7.25%	103.55	5.70%

## Money Market

Throughout the week there was increased activity on GOJ notes and higher market liquidity. The GOJ reopened its 2025 and 2037 Benchmark Investment Notes to raise J\$4B and J\$2B, respectively. Both notes were oversubscribed with the 2025s and 2037s receiving offers totaling J\$6.67B and J\$4.77B, respectively. The GOJ continued to employ the reserve yield strategy, where a cap is placed on the maximum bid yield for each Note. The 2025 Note was capped at 8.5% and 2037 Note was capped at its coupon, which was 10%.

As at the 27th of October, a total of J\$26.1B was in the market, as represented by the BOJ's aggregated current balances. The aggregated closing current account balance increased by J\$17B from J\$9.16B on October 20th. The increase in the balances at this time of the month is not unusual, as DTIs see inflows for salary payments. However, in general JMD liquidity remains tight, leading to further high levels of competition for cash by market players; consequently, rates are expected to remain elevated. Market players were mainly square last week and overnight lending was limited. The average yield from BOJ's competitive price auction declined to 7.68% relative to 8.67% in the prior week. The auction was oversubscribed. Bids received totaled J\$24.98B relative to offer size of J\$12B. The highest bid rate for full allocation was 7.75%.

The USD money market remains stable and moderately liquid. Broker market demand for USD remains at 30-days and longer-tenured funds, with some brokers offering as high as 5.50% for one year to clients. There were no interventions from the BOJ in the FX market last week.

# Recommendations

Ticker	Closing Price (Oct. 31)	P/E	Avg. Sector P/E	Current Recommendation
WISYNCO	\$17.77	16.5x	15.3x	BUY
LAB	\$2.66	16.6x	29.5x	BUY
GK	\$83.73	10.0x	10.3x	BUY
TROPICAL	\$2.72	21.3x	18.2x	HOLD
ELITE	\$3.48	24.9x	29.5x	BUY

# Dates to watch this week

■ International ■ Local

October-November 2022				
MON	TUE	WED	THUR	FRI
<b>31</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>
Euro CPI (YoY) (Oct)	MailPac AGM	US Fed Interest Rate Decision	UK Fed Interest Rate Decision	US Unemployment (Oct)
	UK Manufacturing PMI (Oct)			

## Regional News

### Tourism Still Driving Barbados Economy (Nation News)

Tourism is leading the way as the Barbados economy continues its recovery from the COVID-19 pandemic. Central Bank Governor Cleviston Haynes reported in his third-quarter economic review that the economy grew by 10.1% in the first nine months of this year, including 9.8% growth between July and September alone. The forecast is for the economy to grow by 10% this year overall, followed by growth between 3.5% and 5% in 2023. However, Haynes said that predicted slower global economic activity amid the tightening of financial conditions in advanced economies was a threat to Barbados' prospects.

The Governor said that while the economy was not yet producing at pre-pandemic levels, "based on encouraging forward bookings, tourism is expected to sustain its rebound for the remainder of the year". Importantly, visitor arrivals "continue to be dominated by the traditional source markets, with the United Kingdom leading the way, accounting for 40% of total arrivals and 71% of 2019 levels". This outpaced the recovery from the United States and Canada which had arrivals of 56% and 49% of 2019 levels, respectively, for the nine months, he noted.

Haynes said that as Barbados' economic recovery continues, the government needed to continue its reforms, particularly of state-owned enterprises. "These reforms are intended to improve the quality of service while reducing the burden on the public finances and freeing up resources for needed infrastructural developments and improved resilience to climatic events," he said. Most notably, better service quality in the public sector should also contribute to the overall enhancements in productivity and competitiveness in the private sector.

### Slowdown In US Growth To Widen The Dominican Republic's Current Account Deficit In 2023 (Fitch Solutions)

Fitch Solutions forecasts that the Dominican Republic's current account deficit will widen to 4.1% of GDP in 2022, down from its previous forecast of 4.4%, as tourism arrivals and spending surprised to the upside. Throughout the year to August, total foreign tourist arrivals have grown a robust 66.9% y-o-y, with stronger-than-expected inflows of French and Spanish tourists underlying this trend.

However, economic slowdowns in key source markets, particularly the US, will slow tourism growth, goods exports and remittances inflows, further widening the current account deficit to 4.3% of GDP in 2023.

Inflationary pressures and tightening financial conditions will cause US growth to slow from 1.8% in 2022 to 0.3% in 2023. Furthermore, given that the US imported 55.3% of all Dominican goods in 2021, dominated by consumer electronics, tobacco products, and medical devices, easing demand from the US will cause Dominican goods export growth to slow to 3.4% next year.

That said, import growth will also decelerate next year, to 3.0%, as prices for raw materials and gasoline moderate, limiting the growth of the goods trade deficit. Similarly, service export growth will ease to 1.9% in 2023, primarily due to weakening tourism demand from the US, Canada and the Eurozone markets as global growth slows.

After strong growth in 2020 and 2021, Fitch expects the contraction in remittances in 2022 will continue in 2023, underpinning a 0.9% decline in the secondary income account surplus to USD9.6Bn, from USD9.7Bn this year.

If the US economy continues to experience persistent inflationary pressures, the US Federal Reserve may decide further tighten the interest rates beyond the current expectations of 4.50% by end-2022. This would likely cause a further weakening of growth in 2023, which would in turn weigh more heavily on Dominican export growth and remittance inflows than currently expected, resulting in a wider current account deficit.

## International News

### U.S. GDP Accelerated At 2.6% Pace In Q3, Better Than Expected As Growth Turns Positive (CNBC)

The U.S. economy posted its first period of positive growth for 2022 in the third quarter, at least temporarily easing recession fears, the Bureau of Economic Analysis reported Thursday, Oct. 27.

GDP, a sum of all the goods and services produced from July through September, increased at a 2.6% annualized pace for the period, according to the advance estimate. That was above the Dow Jones forecast of 2.3%.

That reading follows consecutive negative quarters to start the year, meeting a commonly accepted definition of recession, though the National Bureau of Economic Research is generally considered the arbiter of downturns and expansions.

The growth came in large part due to a narrowing trade deficit, which economists expected and consider to be a one-off occurrence that won't be repeated in future quarters.

GDP gains also came from increases in consumer spending, nonresidential fixed investment and government spending. The report reflected an ongoing shift to services spending over goods, with spending on the former increasing by 2.8% while goods spending dropped by 1.2%.

### IMF Chief Wants Central Banks To Keep Raising Rates To Hit 'Neutral' Level (Reuters)

International Monetary Fund chief Kristalina Georgieva said on Wednesday that central banks should keep raising interest rates further to fight inflation until they hit a "neutral" level, though in most cases they have not reached this point.

Speaking to Reuters in Berlin a day before the European Central Bank is widely expected to raise rates by 75 basis points, the fund's managing director said it would take until 2024 for the positive effect of central banks raising rates globally to be felt.

The ECB had for months said that its first step will be to raise rates to a neutral setting, where it was neither driving nor restricting growth, but some policymakers are now advocating more aggressive action, saying the ECB should go further to tame inflationary pressures.

"At this point, we look for getting to a neutral mode, and in most places, we are not quite yet there," Georgieva said in an interview. Central banks have to bring rates up because "when inflation runs high, that undermines growth, it hits the poorest parts of the population the hardest."

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