KTS CAPITAL MANAGEMENT

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Real purchasing power

- The economist, Mr. Alfonso Peccatiello, confirms numerically our theory that citizens are losing purchasing power over time.
- The chart shows the comparison over the last 10 years between real wages and short term real interest rates in the US. The result is 0%. Therefore, we can affirm that US citizens increased their purchasing power by 0%. Now calculating a negative real interest on savings from around 1-3% p.a., **compounded over 20 years, citizens are losing 1/4 to 1/3 in purchasing power!**

Source: economist Mr. Alfonso Peccatiello, head of fixed income PM ING

S&P 500 Index measured in gold

- Mr Peccatiello shows exactly the right long term comparison, which is mostly forgotten by today`s investors, because we are talking about a 50 year period. That is over two generations and younger investors are not aware of such a `time` phenomenon.
- The chart below shows the development of the S&P 500 Index vs gold: after 50 years the performance is 0% ! In 1971 U.S. left the gold standard and started freely the creation of new USD (as any other country) and the result is: illusional growth!

Source: Alfonso Peccatiello, head fixed income ING

Inflation numbers

- April's CPI index was higher than expected and jumped 4.2%.
- As they announced last year, the Fed accepts this transitory phase and is not going to increase interest rates. As argued on multiple occasions, the government's high indebtedness is going to be reduced via higher inflation and economic growth, like the US did following WW2.
- Many CPI categories were driven higher by the base effect of depressed prices during lockdown: car&truck rental, gasoline, lodging and airfares, in addition to housing demand (appliances and furniture). Many people decided to drive by themselves, which was safer than public transportation. Also the index of used cars had an incredible jump.
- Such base effects should diminish over the next few months and slowly fall towards 3% and afterwards test the wished for FED target of 2 to 2.5%.
- It looks like there is a supply bottleneck in a few sectors and employers are struggling to recruit enough staff at the moment (explained in our last weekly's report). But, over time, companies will need to increase production and also labor wages, which should be healthy for the economy- and that is actually anticipated by the FED.
- Being a temporary effect and being the FED still under Powell, markets reacted in quite a relaxed manner to the news. But, bonds and also defensive equity strategies (sectors like utility, staples, food&beverage, pharma) are suffering. We noticed that higher quality stocks suffered in favor of more cyclical sectors, which are profiting from infrastructure plans and the normalization process. We believe in maintaining balance in our portfolios, having invested in our best in class value fund Classic Global, our energy and renewable expert Renaud and our best in class Commodity & Precious Metal Fund Bakersteel. But, we maintain still exposure in Alkeon & Co, being a long term investment and having FCF yields and dividends increasing more than bond yields.

Commodities

- According to an article in the FT magazine on the 5th of May, the International Energy Agency (IEA) foresees a **bottleneck in rare metals**, and also **copper, silver, iron and nickel;** which is going to delay the transition to clean energy.
- As always argued, we are invested in silver and in our best in class fund **Bakersteel** to profit from this major bull trend. Our best in class fund with a **long/short strategy in Energy and Renewable Sector** is also well positioned, being long the most attractive commodities and also uranium, tankers, LNG, gold & silver and being short renewable expensive hypes like Plug, etc.
- We have also increased our position in the copper project **NCU CN, Nevada Copper**, because the mine is re-opening underground production and its open pit mine is the only permitted copper open pit in the western world. The company is still reviewing the project`s feasibility study. Management is confident of a major upgrade of resources. According to Glencore (in FT magazine, 6th May 2021), copper prices need to increase an additional 50% for (increased) supply to meet demand. Major copper mines have not invested in the development of new copper projects for over a decade.Therefore, the higher the copper price the higher M&A activities are likely to be. Major mines are going to give priority to acquisitions of already authorised mines with lowest costs (open pit has a much lower cost than an underground mine). Nevada copper mine would be the top on the list and from the summer onwards it will be cash flow positive. Pala Investment, the family office based in Zug of the Russian oligarch Mr. Vladimir Lorikh, invested over 200mio USD to guarantee the necessary financial stability for the mine to go into production and be CF positive. The sum of the parts of the mine is over 2 CAD per share and the upcoming feasibility study should increase further the net present value (NPV) of the shares to over 3 CAD. Market participants focus, for the moment, only on the major mines like FCX, Freemort McMoran but, as we know, when a sector is hyped, investors search for attractive smaller mines as possible M&A candidates.

Cybersecurity

- The **largest U.S. gasoline pipeline** (carries around 45% of the East Coast's supply of diesel, gasoline and jet fuel every day) was subject of a major cyberattack on Friday the 7th of May 2021. The main pipeline was closed for over 6 days and the event is still creating disorder in the local supply chains. Because of bottlenecks in truck transportation, it is very difficult at the moment to compensate for the resulting supply deficit.
- The attack also caused a spike in U.S. gasoline and diesel prices, which partially eased on the 13th of May.
- We find it incredible that such attack could have succeeded, despite the massive increase in cybersecurity innovation. More money needs to be invested in R&D to urgently produce more efficient and robust cybersecurity.
- We also understand from an article in “The Economist”, that these kind of attacks are also a source of profit for the hackers.
- In fact, on the 13th of May, it was announced that Colonial Pipeline Co (the company owner of the pipeline) paid nearly USD 5 mio to Eastern European hackers (apparently the Russian hacker group Darkside) via difficult to trace cryptocurrency payments. Payment was made within hours of the attack, showing the immense pressure the company faced and contradicting early reports that the company had no intention of paying an extortion fee.
- Our best in class fund Alkeon has an exposure in the cybersecurity sector.
- We are actually surprised that the hackers still expected to be paid in cryptos; nowadays, the authorities should surely be capable of tracking and identifying the final beneficiary? No wonder we are reading the headline on the 13th May, that the IRS is probing Binance for money-laundering! We are not sure if the 2 events are linked but, after what happened, we expect a lot more action from the authorities.

Market sentiment

- The momentum ETF ARKK US (CIO Cathie Wood) is not actually managing to hold the important Fibonacci's support level and is breaking down to lower levels. The ETF is -31% YTD and this is a sign of weakness of the market sector, where hyped stocks are all collapsing but the S&P 500 Index is still at its highs. People are comparing the ARK Innovation's weakness to the QQQ in correction mode back in the year 2000/2001. According to this comparison, the downside risk of ARKK US is still substantial. It is difficult to quantify the correction potential but, as argued on many occasions, the valuation of such hype stocks is coming back down to reality. Most of them are still burning cash and the rally was just unsustainable.
- Some market participants are arguing that ARK is no longer outperforming the market following the liquidation of the HF Archegos. Apparently, an unidentified HF was buying the same positions in order to manipulate prices and ARK was also participating in the scheme.

General news

- We learned that Volkswagen had to close production down for 2 days in Chattanooga (USA) due to continued shortages of semiconductors. The analyst of our best in class fund Alkeon told us that semiconductor production has recently being massively increased, therefore, in a few months the supply gap should be closed. Therefore, there is no risk of a collapse of certain sectors. In the short term, because of this massive increase of production, commodity prices should still keep rising.
- We are also pleased to read that South Korean Samsung is boosting its spending by 30% to USD 151 bio through 2030 and Hynix is committing USD 97 bio to the expansion at its existing facilities, in addition to its USD 106 bio plan for 4 new plants in Yongin (total more than USD 450 bio investments in new chip manufacturing in the next decade).
- We are also reading from multiple sources that the increase of work from home during the pandemic is causing the near collapse of the 4G network The world desperately needs the new 5G network capacity, in order to manage the substantial increase of data volume.
- We were very surprised to read that the performance of the speedboat producer Brunswicks rallied much more than the tech giant Google, since March 2020. It appears that, during the pandemic, everyone bought a boat and went out to sea!
- Disney hit 100 mio subscribers and is quickly catching up with Netflix (204mio). Netflix needed around 4 years to reach 100 mio subscribers, Disney did it in less than 1 year. Probably, Disney is profiting from the cartoon side for kids!? We do not believe the 2 providers are in direct competition. Disney is complementary to Netflix for families with kids.
- The cannabis sector is still in a correction mode, but M&A activities are picking up. The company Trulieve (TCNNF US) intends to acquire Harvest Health.

Bitcoin news

- Palantir now accepts bitcoin payments and is thinking about Treasury investment.
- Elon Musk has said that Tesla will stop accepting bitcoin for car purchases, citing environmental concerns (blaming insane energy consumption). Actually, we should be concerned about the credibility of Elon Musk himself, because two weeks ago Tesla sold a substantial part of its bitcoin's position arguing it was to test liquidity of the crypto market; and now it was perhaps for a different reason!? Everyone knows the dilemma of crypto's environmental impact. Mr. Musk knew it before buying a position in bitcoin. The crypto space is not under supervision by the authorities, therefore, everything is allowed; but if a person loses credibility once, it is very hard to restore it.
- Market participants are speculating that the eco friendly crypto Cardano could be the winner of Elon Musk's comments.
- The ARK fund manager Cathie Wood invested 2 bio USD into the Swiss based crypto provider 21Shares. 21Shares platform is in fact offering the best instruments to trade crypto currencies, with good liquidity and at very good spreads.

UBS want to offer crypto to wealthy clients

- UBS is exploring ways to offer cryptos to wealthy clients but, apparently, the plan is still at the early stages. There is a common joke in Switzerland, whereby market participants used to say- when UBS “jumps on the train”.....it is just too late!
- There is also a good reason for saying as such. Looking back over the years reveals that UBS started to offer services of thematic or sector funds at the peak of the trend. For example, when UBS launched the New Market Fund back in 2000, the manager found himself with a lot of liquidity to be invested, but no attractive stocks to buy. Therefore, he started to “push” the price of hyped stocks to new highs and soon afterwards his hyped holdings collapsed.
- Not to mention the real estate venture at the peak of the market. In fact, UBS’s clients still have, in their portfolios, real estate fund positions in liquidation after more than a decade. Meanwhile, the bank has launched new real estates funds and started all over again.
- In 2007, just before the financial crisis, UBS launched a new “absolute return fund”, which collapsed in 2008. In 2010 the Swiss company Swatch sued UBS winning in court (compensation of CHF 30 mio), because UBS failed to properly disclose the risks.
- And recently the scandal in the U.S. linked to the UBS`s yield enhancement strategy; UBS is defending a substantial lawsuit.
- Moral of the story: people`s tendency is to forget quickly the big mistakes made by major providers. The danger is that history can, and does, repeat itself. We understand the pressures on the banks to launch these products to avoid being out of the game for too long. But, this is exactly the reason to explain why major banks keep making the same mistakes. Mistakes that cost a lot of their clients`money. The cause is lack of innovation and not being able to analyze early the potential of new technologies or trends. Consequently offering such products when market sentiment is at peak momentum, which is typically the best time to sell.

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