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KTS weekly update Nr. 30

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Valuations

- We read in most research publications that market valuations are at bubble levels and it is only a matter of time before the bubble bursts.
- Such assertions are based on indicators such as Warren Buffet`s Index (global market cap/global GDP), P/E level at 1 standard deviation to average (but actually P/E`s are lower than pre pandemic, because earnings have substantially increased), length and magnitude of the equity market rally after Covid19, leverage of margin debt, the level of equity allocation of retail investors and the highest level of analyst buy recommendations. And, finally, the level of central bank balance sheets.
- Mr. "the big short" Micheal Bury is shorting Tesla and Ark ETFs (Cathie Wood), whilst actually being long Alphabet and Facebook.
- We no longer analyze such historical statistics, because we genuinely believe in the new central bank paradigm. Should the situation evolve as it did in Japan, it could last over 30 years. With the injection of 3-4x more liquidity into the market than GFC 2008 by central banks and ongoing huge stimulus packages from governments (U.S. House just passed USD 3.5 trillion Biden budget blueprint for domestic infrastructure, environment, social, family and health services programs) the global economy has not seen anything yet and the upside potential could be huge. In addition, USD 5 trillion is on the sidelines in US and EUR 7 trillion in Germany. Therefore, there is plenty of cash losing annual purchasing power ready to be invested in one way or the other. We stick with the forecast of our best in class fund Flossbach, whereby markets can easily increase an additional 35 to 50% from todays level and would be still offer fair value.
- Nevertheless, when there is optimism in the market, there is also a lot of fraud. Nowadays, platforms are offering "fancy" projects with illusional performance promises to retail investors. Therefore, the biggest risk for retail investors is actually to believe in the wrong people and invest in the wrong private equities, venture capital or SPACs.

Precious metals’ miners M&A cycle

- Below we can observe a very interesting chart from Mr. Otavio Costa (Manager at Crescat Capital).
- In 2010 the price of gold was at the same level as today and the gold mining sector experienced a tremendous increase in M&A activities. At the time, most gold mines were not even cash flow positive. Today it is different, as most of the gold mines are free cash flow “machines”. Now they have enough liquidity for acquisitions and we should soon experience a pick up in M&A activities.

KTS feels comfortable with the investments in the best in class funds Bakersteel precious metals and Electrum (Source: Crescat Capital LLC)

"Buy on dip" after the pandemic

- Market drawdowns since the pandemic have fallen dramatically and each is less than prior ones. We have lasted 10 months without experiencing a pullback of over 5%. During 2016 to 2018, the S&P 500 Index rose without any 5% pullbacks for 20 months.
- Market participants believe in algorithm models. But, KTS is convinced that the source of the market's support is mainly due to massive share buyback programs (see next slide). The proof is also the fact that, whilst blue chips are still at their highs, momentum stocks are more than 50% lower than February 2021' highs.

S&P 500 Index drawdown in % (source: Flowbank / Thedailyshot)

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The power of share buyback programs

- The below chart from CharlieBilello (via Flowbank) shows the USD 420 billion share buyback program of Apple over the past 8 years, which is greater than the market cap of 489 (!!) companies in the S&P 500 Index.
- Major companies are reaching their highest levels of free cash flow, which is nowadays exceeding the buyback program! This is actually leading to deleveraging and rising cash levels (US companies are sitting on the largest pile of cash ever: USD 2.1 trillion).

Tremendous natural support of markets: huge share buyback programs from blue chips (source: CharliBilello / Flowbank)

China real retail sales growth

- Market participants believe in the strong growth of Chinese consumers, but the economist Mr. Yardeni is pointing out an alarming fact. Due to the historical Chinese “one child policy”, Chinese *real* retail sales growth has been falling since 2011 (following a peak of 18.7% growth) to 0% growth in July 2021. We all know that the Chinese government is aware of this alarming reality and is motivating citizens with all possible means to have more children, but, meanwhile, growth is suffering.

Source Yardeni research

General news

- Mr. Powell`s 4 year term as chairman of the FED ends in February 2022. Apparently, in the next weeks the President Mr. Biden is going to announce either the possible renewal of Mr. Powell`s term, or his replacement. In our eyes, the best move for Mr. Biden is a renewal. Thereby, to guarantee that the FED is fully synchronized with the massive stimulus package of the Democrats.
- Globally, many citizens are still battling against the vaccination of Covid19. Meanwhile, Modern's mRNA HIV vaccine is about to start human trials. We all knew that the mRNA technology was game-changing, but we were not expecting a vaccine against HIV. Everyone can guess in which direction we are going.
- The exposure of Blackrock ETF to the Chinese market is "only" 2.6% of total funds managed, but other providers (Vanguard, Invesco, etc.) is even lower. Therefore, overall exposure to China is still quite insignificant and after the tremendous correction from the highs (-57%) it could be, for long term investors, an attractive entry point (at the moment more via "cash in" of volatility, like selling put options). In fact, China`s market experienced the largest drawdown since 2012 and, historically, after such a correction the market could rebound over a 2 year time span. In our eyes, Chinese authorities reached their goal to have the most influential billionaires in the country aligned with their politics. Therefore, after the crackdown, everyone in China is going to focus on restoring confidence. Of course, it is a long process but valuations are compelling and it is worth the risk.
- The education department in U.S. will cancel student debt for more than 320k borrowers, this is the equivalent of USD 5.8 billion in student debt forgiveness! Another nice way from the state to write a "blank check" to the "middle class".
- India's government wants to monetise state-owned assets. We are checking with our best in class fund Aubrey Emerging Market to see if they are anticipating attractive investment opportunities. Or fear that India`s state companies could be corrupted, lack transparent bookeeping and ignore best practice compliance policies.

Crypto currency news

- Back in June, the UK banned the cryptocurrency exchange Binance. But, today PayPal will allow customers in the UK to trade and hold bitcoin and other cryptocurrencies. PayPal is going to compete with rival platforms such Coinbase or Revolut.

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