KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 33

The 17th of September 2021

Asset classes

- Since 2007, Yale's endowment fund has seen a shift in its allocation from real assets and US stocks into private equity, venture capital and also bonds. KTS also recognizes the need to diversify a part of its asset allocation into these sectors. We invested a small holding into the innovative Croatian private company Rimac and the Fasanara Venture Capital Fund (with main focus into Fintech), both have tremendous upside potential.
- As argued in the past, financial providers are catching the momentum of ESG and sustainability investments. But a proper and in depth analysis of these providers is needed, because whenever there is hype there is evidence of fraud and unprofessionalism. On the 25th of August U.S. authorities were investigating the German asset management DWS (arm of Deutsch Bank) after the firm's former head of sustainability said it overstated how much it respected sustainable investing criteria to manage its assets. The SEC is continuing to "hunt" for dubious ESG labels and, honestly speaking, we also question how suddenly USD 35 trillion can be invested into the ESG sector in such a short period of time and ask whether all the providers have the appropriate investment ESG process. We are constantly monitoring our best in class funds, but ethics and sustainability have always been integrated into our investment process. Therefore, we are confident that we are invested in professional managers, who always respect an ESG investment process. Recently, their investment processes have been updated according to the latest standards.
- We also have to mention the risk of an overcrowded space, when the entire world is moving into the same "corner". Therefore, we also invest in managers focussing their investments into companies which are in a transition phase to become "greener". Our experts are especially focussed in the energy and material space, which are the most attractive sectors in term of valuation vs historical averages (still very low, whilst other sectors are at their peak). Many companies are certainly improving their ESG standards and the market should compensate such efforts with higher multiples.

Passive investments

• An additional hidden risk for equity markets is the continuous rise of passive investments. As argued recently, we fully agree with market participants on the fact that only few (apparently less than 15%) active managers are beating their benchmark over 5 years. But, we are also aware that the market is in a “Fugazi” paradigm, whereby most investors are disillusioned to believe they understand perfectly what is going on. However, everything is based on a very fragile balance and the “unforeseen”, or so called “Black Swan” event, will always be with us. Therefore, we feel comfortable only with those active managers which offer some kind of downside protection. KTS also “calibrates” our general risk with put options, when we think that our equity allocation is too high compared to economic fundamentals. It is obvious that such hedge strategies cost performance points, especially when markets only rally, but investors should not forget that these hedge positions become priceless in panic events, like Covid19.

The shift towards passive funds still trending higher (source Flowbank)

Carbon futures

- Carbon futures keep rising and are now at new highs since they started trading in 2008. Carbon permits under the EU emissions trading system rose above EUR 62/ton reaching an all-time-high.
- For this reason, energy and material companies and also airlines are massively increasing investments in the green space.
- The recent example is the announcement of Chevron and one of KTS's stock picks Gevo to enter into a possible partnership with the aim to develop an environmentally friendly production process of jet fuel from corn, and also for car's gasoline.
- In reality, this is a forced move on the giants in the energy sector, because the Biden administration just announced its intention to reduce aviations carbon footprint 50% by 2050 and 20% by 2030. We also would like to remember the Netherlands' court verdict, which ordered the oil giant Royal Dutch to cut CO2 emissions 45% by 2030 compared with 2019 levels. These are huge and costly moves even for energy giants, which are running out of time and do not yet have enough in house innovation to reach such targets. Therefore, JVs with possible start ups like GEVO are the only reasonable way forward.
- Chevron will go towards building and operating one or more new facilities using Gevo's proprietary technology to produce the fuel and renewable blending components for low carbon motor gasoline and SAF for airline.
- Chevron will co-invest with Gevo and hold the right to offtake 150mio gallons per year. In addition, Chevron has warrants to buy up to 15 mio shares of Gevo with a minimum strike of 8.5 USD.
- The agreement is, at the moment, only in form of a "letter of intent" and is subject to negotiations of a definitive agreement. Of course the path is still long, but this announcement is definitely a game changer showing the direction for the whole energy sector. The alternative would be to buy CO2 certificates.

Sale electric vehicles

- Research of the World Economic Forum shows how Scandinavians are well ahead worldwide in buying electric cars.
- In fact, Norway is at the top worldwide in buying new cars “plug-in”, which means hybrid or all-electric. 75% of new sales were plug-in and 54% of total sales were fully battery powered. The Norwegian government pays generous tax incentives to electric vehicle owners.
- Norway is followed by Iceland, where 45% of new car sales were “plug-in”. Iceland is also 99% powered by renewables.
- In third place worldwide is Sweden with 1/3 electric car sales over total new car sales, followed by Netherlands (25%) and Finland (18%).
- Globally “plug-in” cars made up 4.2% of vehicle sales last year.

General news

- Many market participants are arguing that the FED will be forced to increase interest rates, because the Taylor Rule (basically the difference between the effective inflation rate or GDP growth vs the desired rate) spread is at such high levels. We are not really following such historical data because, as mentioned recently, the FED has implemented many other arguments in order to find more plausible reasons to avoid increasing interest rates; racial unemployment and food stamps, for example.
- The ECB also mentioned it would start tapering, but we would also argue as did Mizuho Bank, that tapering is not tightening. We posted several facts and statistics recently which show central banks are not in the position to taper too aggressively. Therefore, they are going to maintain a strong QE presence and monetary conditions are going to stay supportive for risky assets.
- We have seen multiple sources comparing Barron’s magazine title on the 3th of September 2021 “Nothing can take the stock market off its record run” with the one in 1929 “Stock Market Invincible” (buy, buy, buy! experts advise). We believe, the situation is not comparable because, back then, the market did not have the full support of global central banks and governments’ stimulus packages, like nowadays.
- The UK labour market is in better condition than pre-pandemic. We can definitely say that the UK surmounted Covid19 and Brexit!
- According to media, the city of Xiamen (4.5 million people), a manufacturing hub for electronic components from companies including ABB, Schneider, is locked down.

Crypto currencies news

- As mentioned in our last report, we believe that El Salvador aims to introduce bitcoin wallets with the final goal to diversify from traditional and expensive payment systems. Like, for example, the global SWIFT payment system, which also has being abused by Americans to implement sanctions.
- El Salvador's President Nayib Bukele also added in an interview, that providers like Western Union and MoneyGram could lose up to USD 400 million a year in commissions for remittances, thanks to the country wide bitcoin adoption. We would add that the amount USD 400 mio could possibly be too high, but the direction is clear and for this reason we genuinely believe that the blockchain technology is slowly, but surely, going to replace actual expensive payment systems.
- An additional proof of the blockchain's innovation and evolution is recent FINMA approval for stock exchange listing and a central securities depository for the trading of tokens (so-called distributed ledger technology DLT). FINMA has authorized SIX Digital Exchange AG to act as a central securities depositary and the associated company SDX trading AG to act as a stock exchange . Therefore, FINMA recognizes the innovative potential of new technologies for the financial markets. Basically SIX is going to be a regulated exchange differentiated from the actual platforms like Binance, Kraken, Bitfinex, which are not regulated.

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