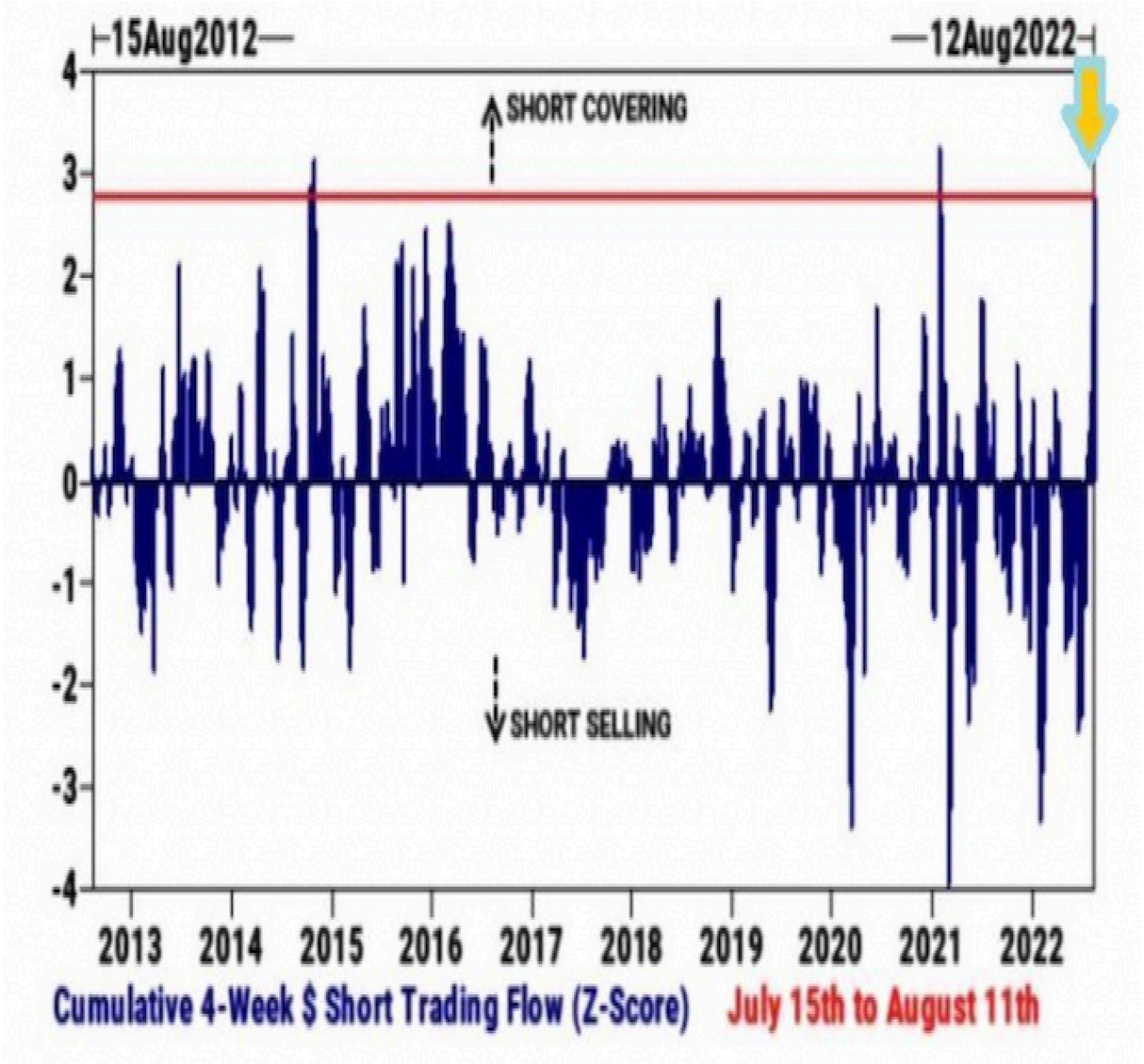
KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 33

The 19th of August 2022

3rd biggest hedge fund short covering event in the last decade

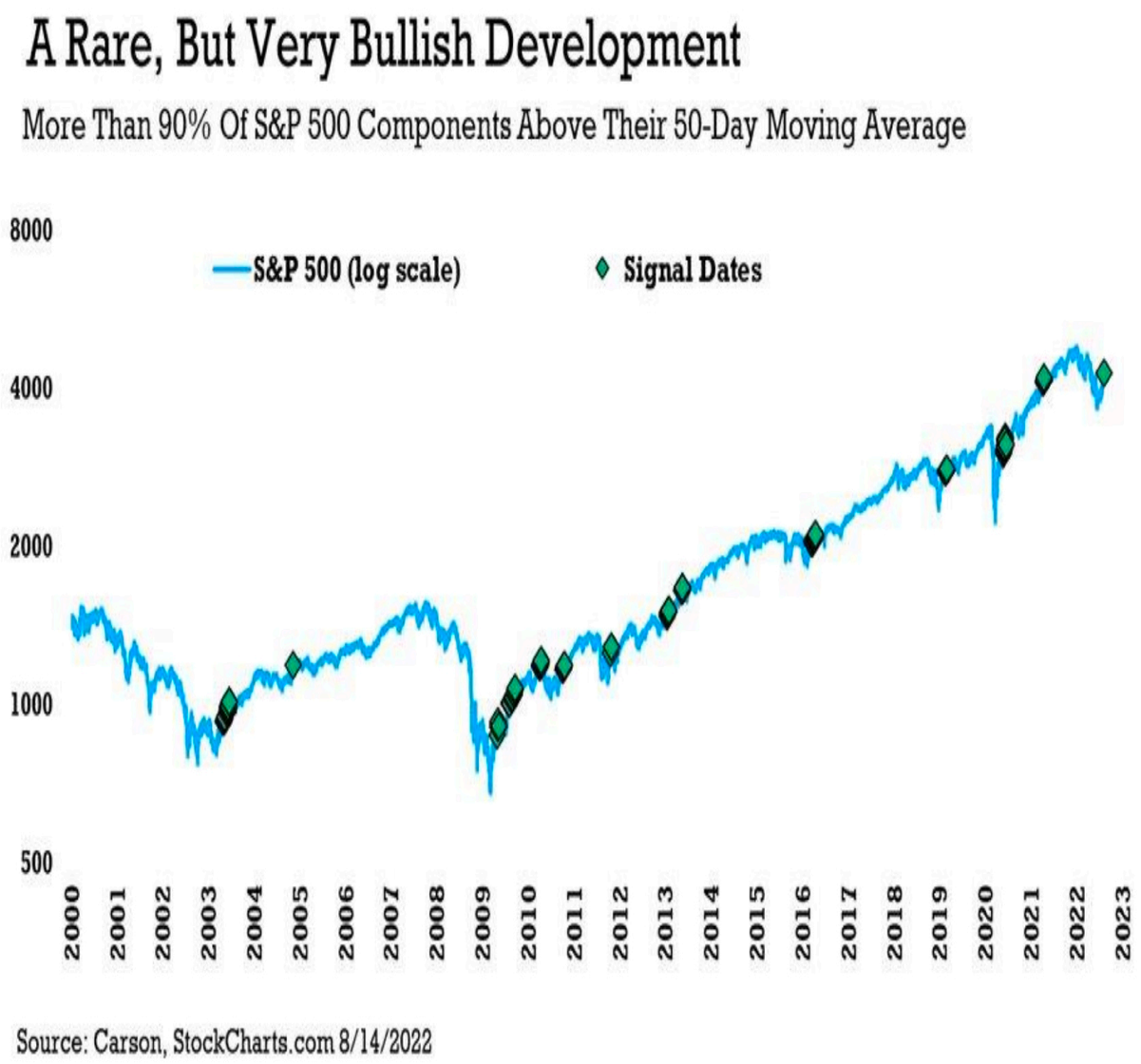
- According to GS Prime, apparently the actual rally has now become the **3rd biggest hedge fund short covering event in the last decade.**
- If it is true, most probably equity markets would have a capped upside potential in the next 2 months?!
- Also Mr. Excell is explaining in his weekly market update, that probably the rally went a bit too far for the moment, with the credit market not buying this move, multiples have expanded back to the higher end of the range, and technically we are getting stretched. Mr. Excell is not expecting a correction, but a **sideway equity market at least until the Jackson Hole Symposium at the end of August.**
- Meanwhile, **mutual funds have the highest percentage in cash, higher than during the Covid pandemic**. According to the chart of GS, cash % of total assets is 2.4% from 1.4% at the beginning of 2022, **therefore, sooner or later and before year's end, this liquidity is going to be invested,** especially with Democrats back on the game with 60% approval rate.



Source: GS via Syz Group

Over 90% of S&P 500 components are now above their 50-day mov average

- On the right-hand chart, courtesy Carson, StockCharts.com via Syz Group, we can analyze how **such event is rare, but with very bullish development.**
- On Friday, the 12th of August, **more than 90% of the S&P 500 components were above their 50-day moving average and historically, such signal triggers a strong uptrend.**
- During the rebound from June 2022, the **best performers were "meme" and non-profitable stocks,** and also crypto currencies like Bitcoin, but especially Ether, having the upcoming "Merge" upgrade in September.
- Taking into consideration that the **majority of professional investors are underweighted equity, overweighted cash and conservative sectors**, equity markets will rally further before years' end, most probably after US elections in November.
- We have to admit that, reading Mr. **Michael Burry liquidated the entire portfolio at the end of Q2** and just holding 1 stock, a private-prison operator Geo group, is not comforting.



Source: Carson via Syz Group

Selling in panic during an equity market's decline

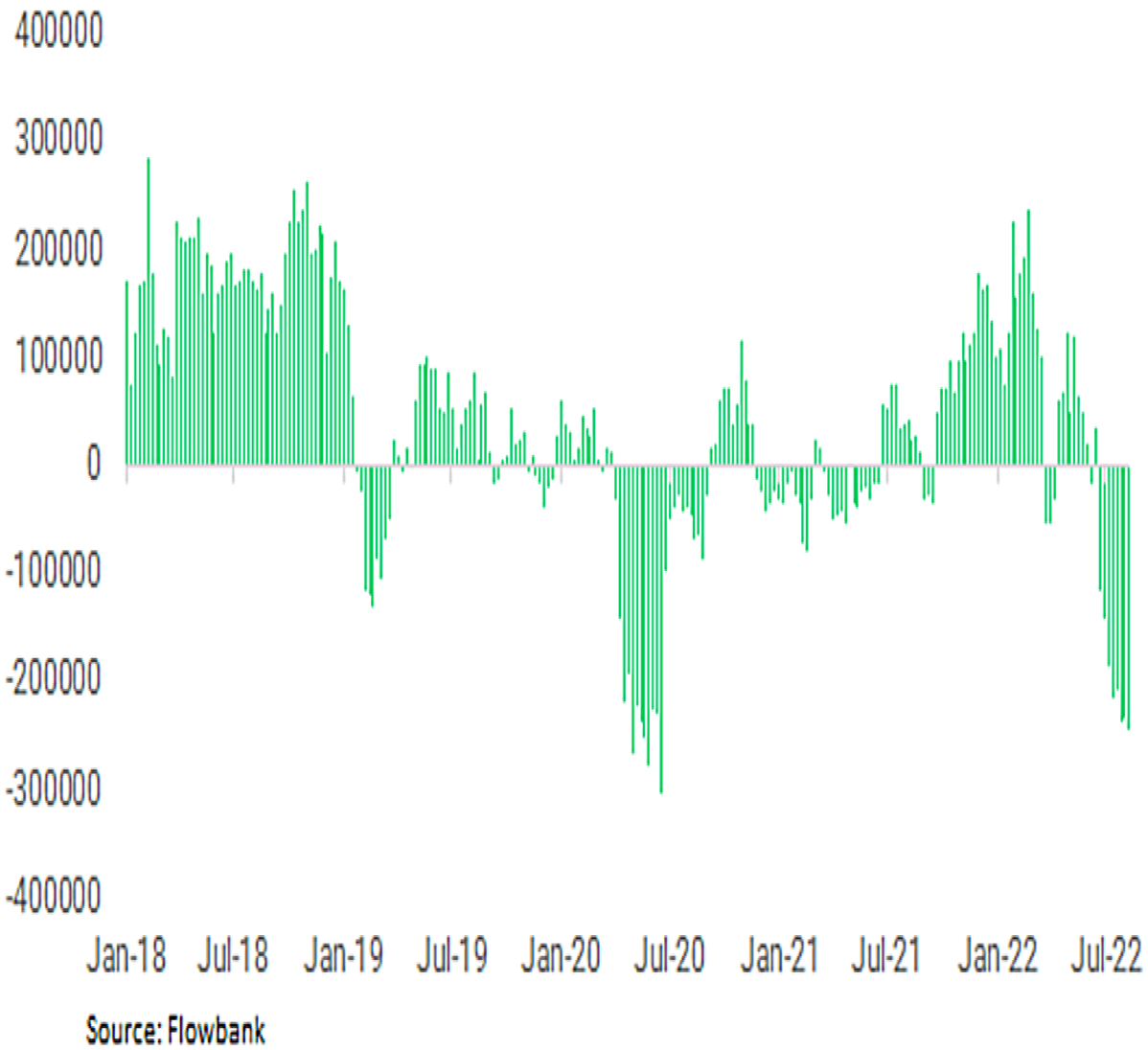
- On the right-hand chart, courtesy dhaval_kotecha via Syz Group, shows on the long term, that investors selling in panic during equity market' corrections are at the end the real losers.
- It is going to be the case also during 2022 behavioral finance and emotional reactions, which is going to cost performance to many investors on the long term?
- **On the statistic we can analyze, when equity markets corrected on average 29%, the upside potential over 5 years is +110%**

Year	Crisis Event	Market Correction	5 years +
1956-1957	Suez Canal Crisis	-18%	**100%**
1962	Cuban Missile Crisis	-22%	**87%**
1967	6-day war in Israel	-22%	**85%**
1970	Recession	-33%	**47%**
1973-74	Oil Shock / Recession	-48%	**106%**
1979	2nd Oil Shock	-18%	**106%**
1982	Recession (interest rate 15%)	-24%	**240%**
1987	Stock Market Crash	-36%	**104%**
1990	Recession / Iraq War	-13%	**121%**
1997-98	Asian crisis	-21%	**28%**
2000-2002	End of the techno bubble	-50%	**98%**
2008-2009	Financial Crisis / Recession	-56%	**207%**
August 2011	European crisis	-19%	**107%**
March 2020	Coronavirus crisis	-30%	**?**
Average		-29%	**110%**

Dhaval kotecha

S&P 500 Index net non-commercial futures

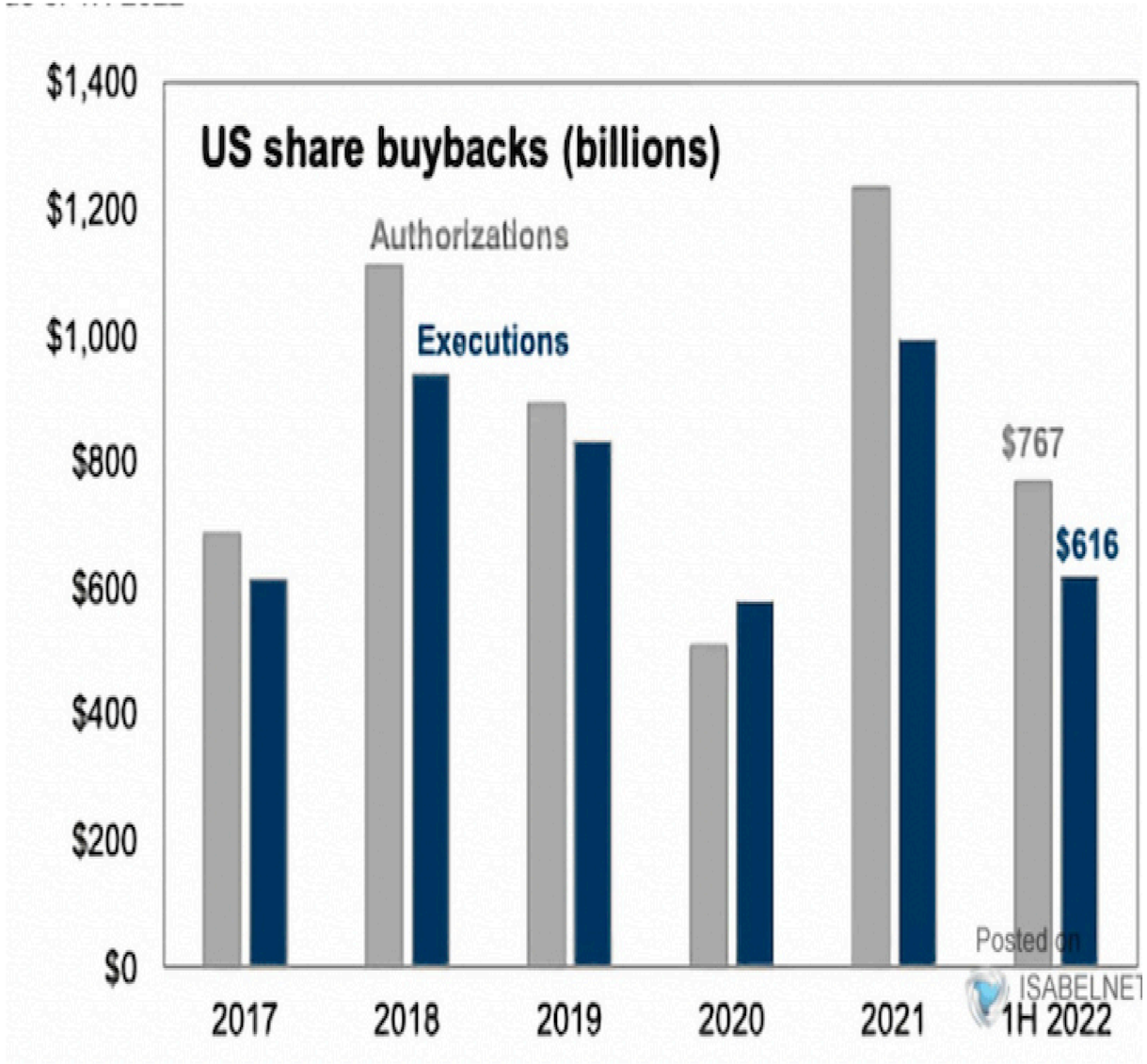
- The right-hand chart, courtesy FlowBank, shows how the **investor's positioning on the S&P 500 net non-commercial futures is almost the most bearish since March 2020.**
- In addition, **investors have been increasing their bets against the S&P 500 Index which rallied 17% from its lows in mid-June.**
- Therefore we can assert that investors believing that a recession is imminent and rate hikes will push earnings down significantly, increased their "bet" during the rally.
- We agree that **equity markets are probably overbought on the short term. The S&P 500 Index reached the resistance at the 200d mov average** and Friday we have the option maturity day, thereafter equity markets will need to consolidate.
- We admit, that fundamental economic data are suggesting, not all negative news are gone yet and therefore KTS is also cautiously optimistic and still focussing on limiting the downside risk, especially in the next 2 months.



S&P 500 net non-commercial futures (source FlowBank)

Volume of share buyback programs

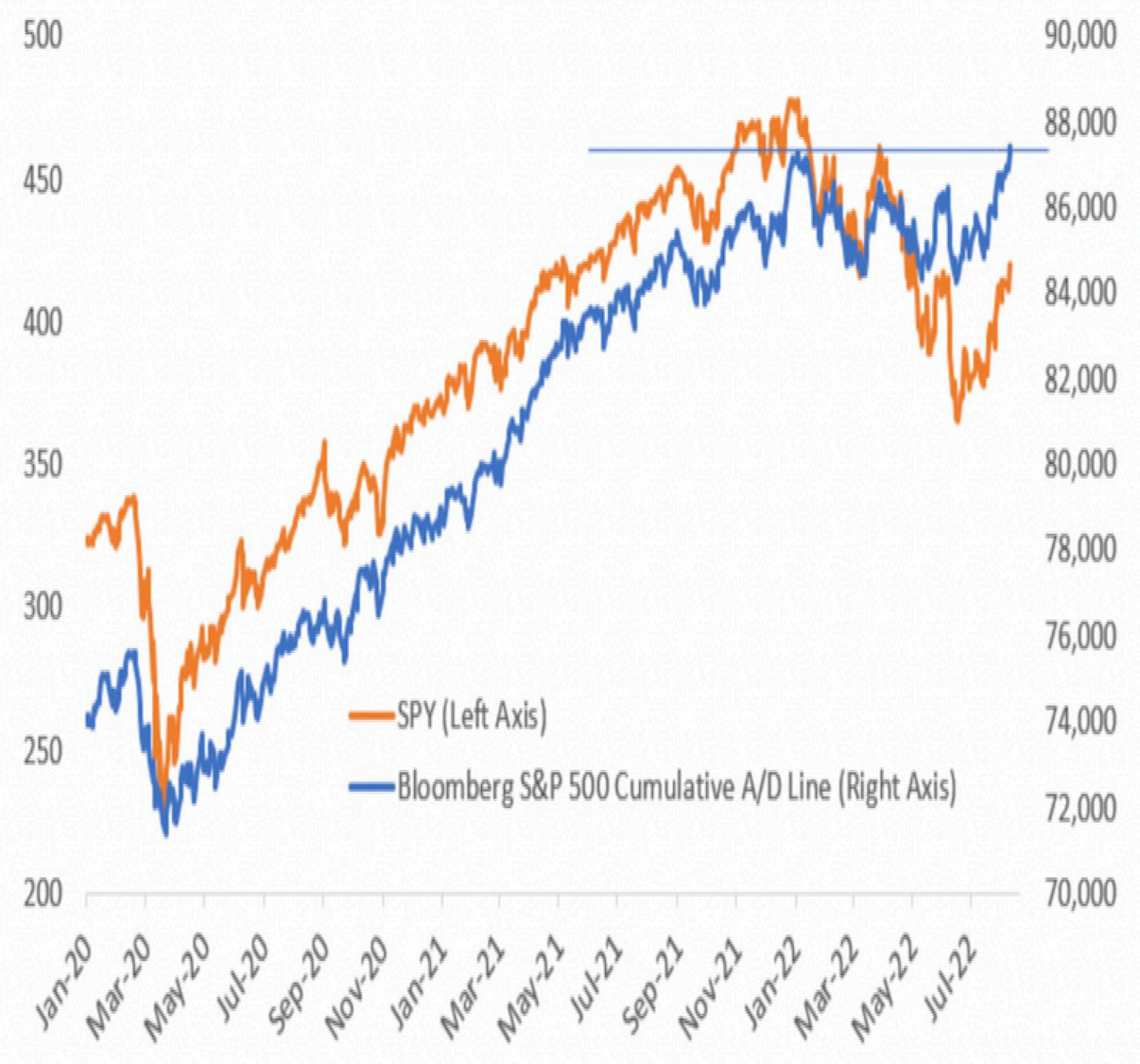
- On the right-hand chart we can notice, how share buyback programs are going to surpass the volume of 2021. On the chart we can analyze **the volume as of 1H 2022: USD 616bn.**
- According to the statistic of GS, buyback authorizations through **2Q 2022 totaled roughly USD800 billion.** Adding 800bn to the 616bn already executed, we would reach a **total of USD 1'416bn for 2022.** During 1H 2022, authorizations were for USD 767bn, but only USD 616 bn were executed.
- As always argued, **shs buyback are the natural support of markets** and during corrections, companies can increase them limiting the drawdowns. **On top: USD 500 bn dividend paid!**
- Having most of professional investors underweighted equities, but ongoing share buyback programs, the risk of FOMO is increasing, especially in the months of November-December, where asset managers need to improve performances.
- **https://www-nytimes-com.cdn.ampproject.org/c/s/www.nytimes.com/2022/08/13/business/stocks-climate-bill-tax-1-percent.amp.html**



Shs buyback+dividend: 2 trillions! Source: Goldman Sachs (via Mr. James W.)

Positive divergence between market breadth and price

- The right-hand chart, courtesy Mr. Budelmann CIO at Bergos AG, is showing how the **Bloomberg's cumulative A/D line made new highs and therefore this represents a significant positive divergence between breadth and price.**
- The A/D line indicator adds up the daily number of advancers minus decliners over time and is used to gauge underlying breadth during rallies and declines.
- According to Mr. Budelmann, there have only been **4 other periods over the last 20 years where the A/D line made a new 52-week high while the index itself was still more than 5% below its 52-week high**. These were:
  - **June 2009, March 2016, April 2018, January 2019**
- Forward performance following those prior breadth divergences has been universally positive over 1,3,6,12 months
- The technical analyst of Julius Bär is also confirming the strength in A/D line, as also the **very bullish market breadth signals, which were not seen since GFC in 2008!**



S&P 500 Index vs cumulative A/D line (source Mr. Budelmann, Bergos AG)

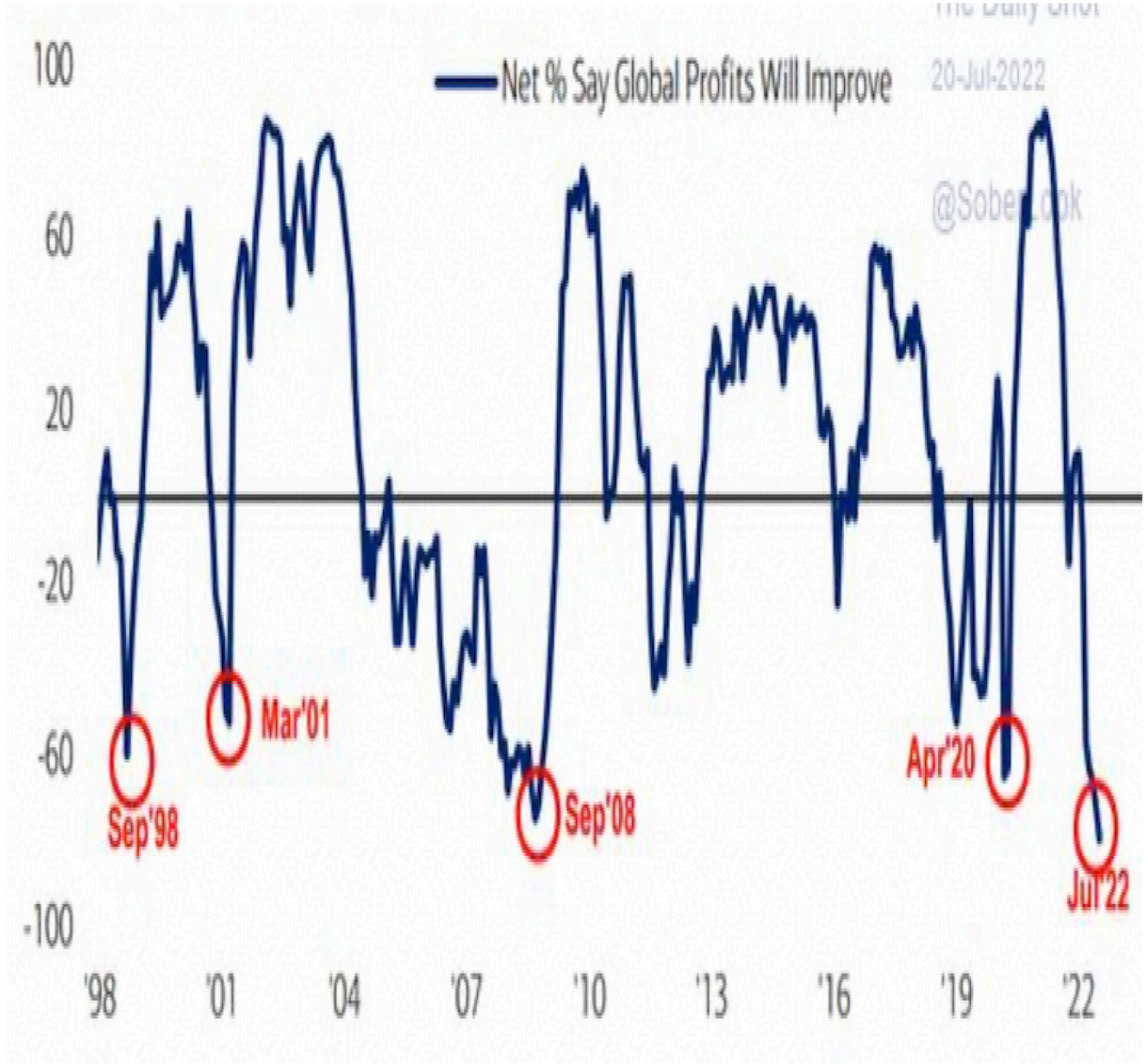
U.S. Households equity holding

- According to the chart of BofA, courtesy Syz Group, U.S. Households are still holding 52% of the stock market.
- Analyzing past market' corrections, equity markets only bottomed a few quarters after significant selling activity from households occurred and therefore market participants are still expecting further corrections.
- **KTS is surprised that retail investors are still fully invested, because analyzing the development of "meme" stocks, cryptos, Spacs, etc. we would assert, that US retail investors suffered the drawdown of equity markets and similar risky assets at the same magnitude of the tech bubble in year 2000 and the GFC in year 2008.**
- The chart indicates only BofA clients and therefore is not representing the integral retail market anymore. Nowadays, US retail investors are using many other platforms outside the bank system in order to trade stocks and therefore in our opinion, such chart is not meaningful as it used to be in the past.

Source: BofA via Bank Syz

Sentiment on corporate profits

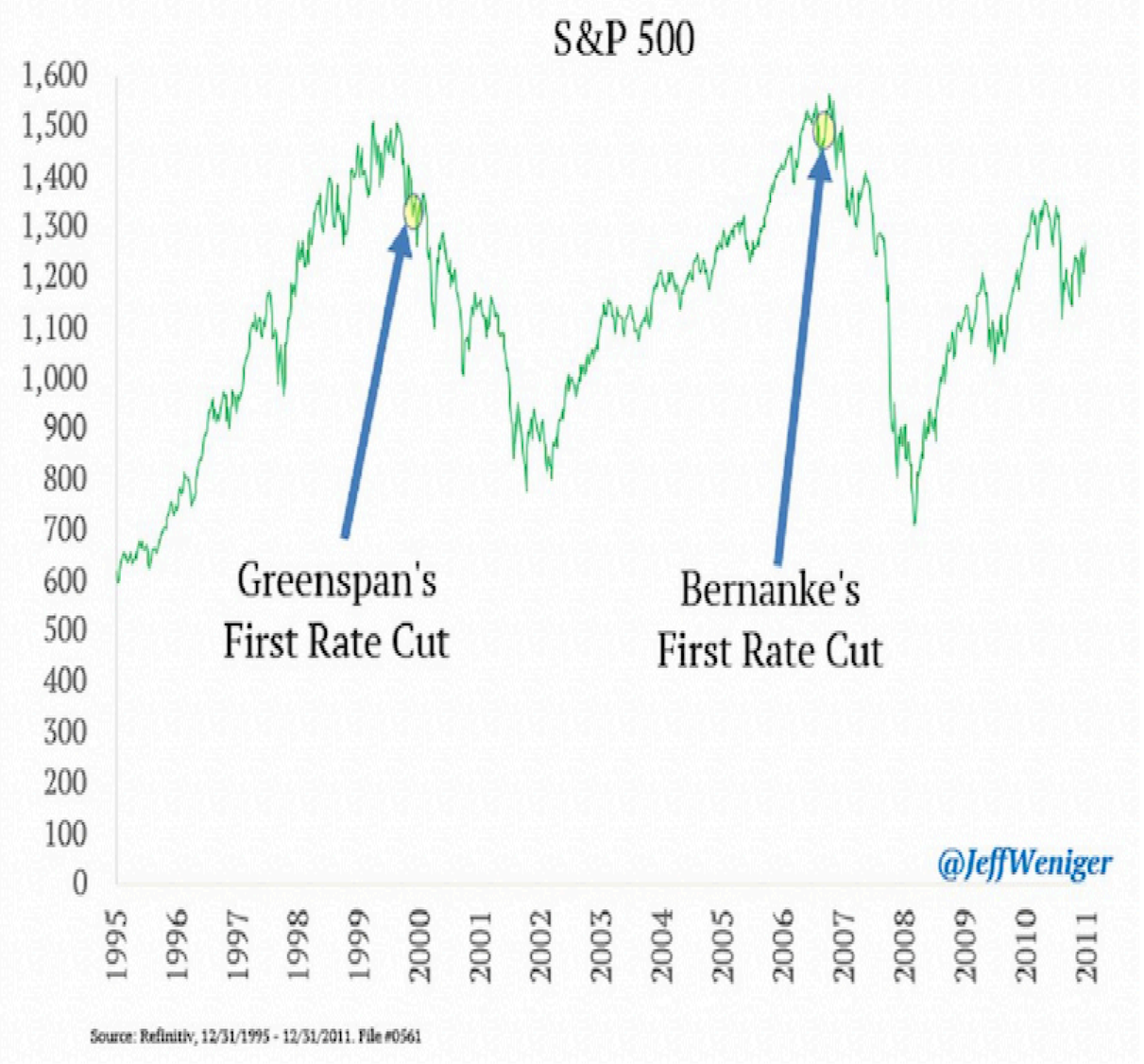
- On the right-hand chart, courtesy Mr. Ansidei, we can analyze the statistic of BofA on **global profit optimism, which is at all time low.**
- The statistic is based on the net percentage of fund managers saying global profits will improve, calculating basically **fund managers' sentiment on corporate profits.**
- **It is not a coincidence that the past lows were on April 2020, September 2008 or March 2001.**
- Therefore we can assert, that fundamentals of the global economy are still negative and **CEOs sentiment is at lowest ever,** but such facts are already discounted by fund managers, meanwhile, as seen in slide nr. 4, share buyback programs are ongoing and in the last decade, **such programs made 40% of the FAANG's performance.**
- The **first rebound leg was the short covering of hedge funds**, as seen on slide nr. 2. The **next leg is going to be professional investors forced to buy again,** most probably after US election in November?



Source: BofA, via Mr. Ansidei

Stock market loves the end of rate cutting cycles

- On the right-hand chart, courtesy Mr. Weniger, we can notice, **how equity markets corrected, when Central banks are starting to cut rates.**
- This is actually logical, because if a central bank needs to cut rates, it means, the economy is in a bad shape.
- It is normally not the case, when central banks need to increase rates, which means, the economy is overheated and central banks need to slow the pace down. But in a **good economic environment, investors can expect higher company' profits**, which should be translated in higher stock prices, as recently showed on the correlation's chart between companies's profit and stock price (see weekly report nr. 32).



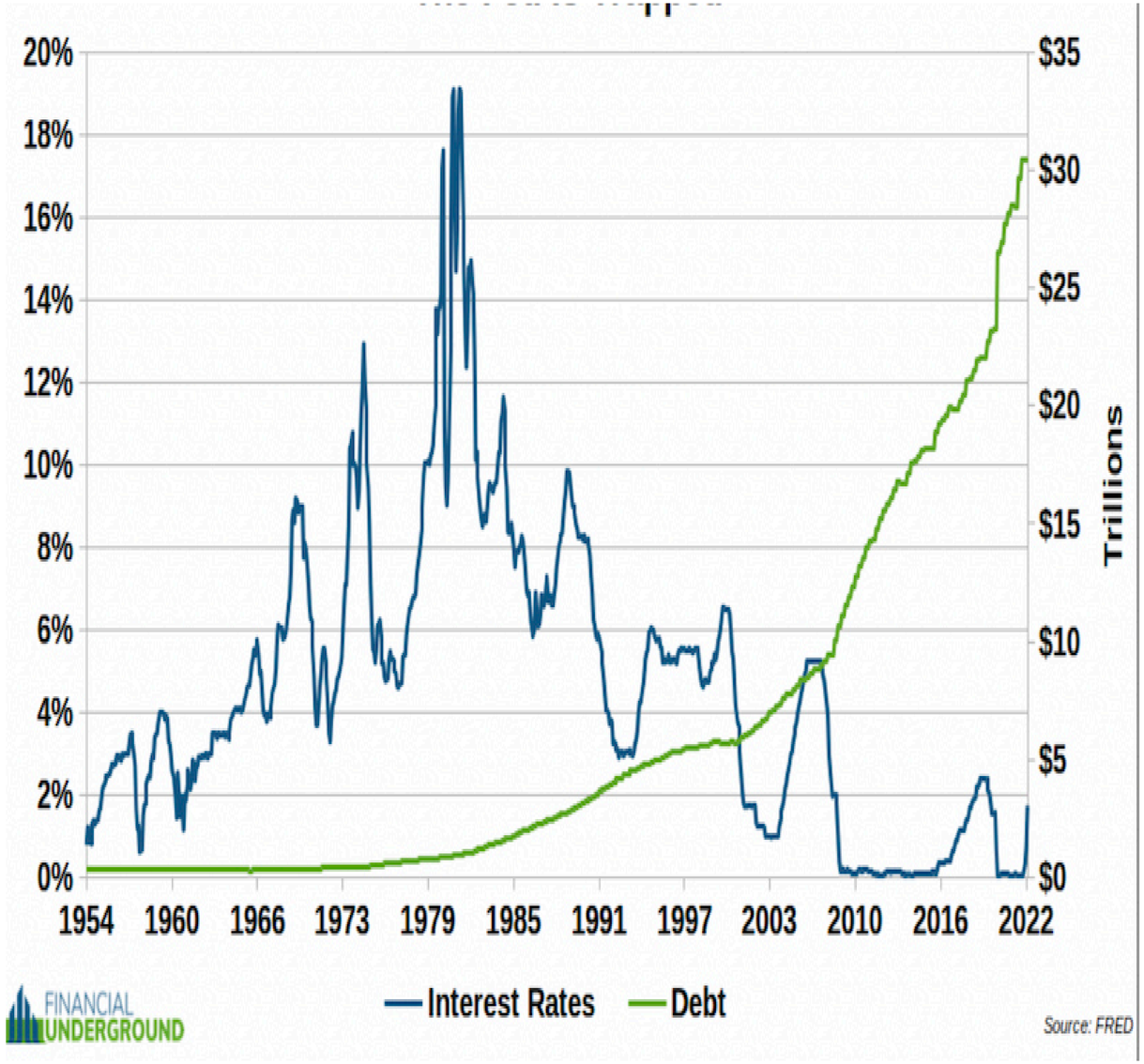
Stock market loves the end of rate cutting cycles (Mr. JeffWeniger)

Macro

- US Empire manufacturing fell from 11.1 to -31.3 and **it has only been worse on 4 occasions**: April and May 2020 (Covid), when it fell -78.5 and -48.5 respectively, twice in 2020 and February/March 2009 when it reached -34.3 and -33.7.
- The National Association of home builders index also fell heavily, down 6 points to 49 from 55 in July and it was the 8th consecutive decline. The index was dragged down by high construction costs and rising mortgage rates.
- **With the economy in recession, economists are already wondering whether the FED can progress with its quantitative tightening program (QT), which is supposed to increase to USD 95 bn a month in Q4.**
- **Mr. Budelmann is showing in his blog the chart of US retail sales nominal vs inflation adjusted affirming, that from April 2021, real retail sales peaked and are now down 1% over the last 6 months!**
- The FED did not provide any specific guidance for future increases last Wednesday, but announced that, they likely would not consider pulling back on interest rate hikes until inflation came down substantially. **Some members are for reducing the pace of rate hikes, others not.** Equity markets reacted slightly negative, but being at overbought levels and having reached the 200d moving average, a consolidation is even healthy. KTS is expecting substantial lower inflation rates in the future and therefore the FED should be in a comfortable situation. On the FOMC of September expectations are for a 0.50 bps rate hike.
- It looks like, **Democrats are back in business.** According to a survey (election betting odds, FTX, Betfair, Smarkets, etc via blog of Mr. Budelmann), **Democrats have a 60% approval rate vs 40% for Republicans.** US elections are going to be held on the 8th of November 2022. This would mean status quo and therefore very positive for equity markets.

The FED is trapped

- A picture is worth a thousand words.
- This chart gives the answer, **how far the FED can increase interest rates, especially on longer maturities**. Basically the **FED can not increase any further**, simply because the US government can not effort it.
- As explained in our past weekly reports, Western governments with high indebtedness are going to **repay debt with high inflation, lower nominal rates and therefore negative real rates and a constant economic growth.**
- Inflation is reducing the real value of the debt and therefore is good for borrowers, specifically big borrowers, like governments.
- Having **pension plans as main bond investors, investors are not going to ask for higher interest rates in addition to the fact, that the FED can step in to close the supply gap**, if needed. We have already experience with Japan, that this is possible and also over a longer period of time.



Increasing debt a low interest rates (Source Financial underground)

European electricity prices spike and possible repercussions

- In France, 1-year electricity prices per Mwh spiked to EUR 602. **The price used to be around 50-100 since 2008 to 2021.**
- Also in Germany we had a similar move and the German Chancellor, Mr. Olaf Scholz, promised a new package of measures, including tax reliefs, to help people with high gas prices.
- Meanwhile, it is official now, that **Germany going to keep last 3 nuclear power plants running** showing a dramatic U-Turn in policy to abandon nuclear energy.
- As recently explained, in our opinion the best way to reduce electricity consumption is to **optimize public buildings and the utilization of lights by public infrastructures.** The electricity reduction's impact would be huge and could solve the actual emergency situation. We have seen, certain German cities (Augsburg was the first one) and also in Spain, started such process and we are confident, more will and must follow.
- Moody also announced, that a squeeze in Russian gas supplies would most probably **imply a credit rating's downgrade of Slovakia, Czech Republic and Italy.** Moody, by the way, already reduced Italy's outlook to negative after Prime Minister Mario Draghi resigned.
- **Economists are raising the probability of a recession in Europe to 60% from 45%,** due to the spike of gas and electricity prices. According to the figures of some economists, **energy's share of GDP is now around 16%, up from 6.19%** a year earlier and therefore is a **10% drop for other purposes**, in addition to a much less productive economy and much weaker GDP, having a weaker GDP but no monetary expansion or lower rates. **Economists are not expecting a mild recession**, **if energy prices are not coming down** and as we have recently analyzed, it does not seem that energy prices are going to fall anytime soon.

European electricity prices spike and possible repercussions

- Last week, we have seen a chart of the bank Lombard Odier, showing that European gas reserves are well positioned for the winter. But other market participants are showing chart of the natural gas storage level in % of capacity, which going to be at 90% at the the end of the autumn, but with the Nordstream pipeline running 100%. We all know, the Nordstream is running only at 20% and therefore even if the storage levels were to somehow get to 90% or 95%, it is still not enough to fell “safe” for the winter. Basically if Russia would cut gas supply, gas reserves would last less than 3 months (statistic of Robin Brooks, HolgerZ via Mr. Monchau)
- The **Rhine water level fell below 40cm,** and therefore not viable for shipping, the **German and Swiss industries will have dramatic delivery issues**. In addition, **nuclear power stations are also running low**, because of missing water in order to cool down nuclear reactors.
- No rain is also a dramatic issue for all European farmers. **But the good news is that we are experiencing heavy rainfall** in France and most probably in the next days also in Europe. This should most probably help to normalize the current emergency situation and **perhaps the panic spike in European electricity prices is going to come back to normal levels,** as it happened with most of the commodities and soft commodities’ prices. We can not quantify, how much of the price’s spike is due to speculation or demand/supply imbalances.
- Meanwhile we are reading that first productions are halted in Europe. The Zinc’s price increased, because Trafigura announced to **halt production next month of the Europe’s largest smelters in Netherlands** (the Budel smelter, controlled by Trafigura Group’s Nyrstar). Also the World’s oldest glass maker Riedel is also going to shut down as the gas crisis deepens.

LNG market and how Europe is taking supply out of poor countries

- Mr. Jain shares in his blog the commentary of the best commodity journalist, Mr. Javier Blas, explaining the actual situation of LNG cargoes to Europe.
- Basically **Europe is outbidding all the LNG cargoes headed to Asia** and therefore poor countries like Pakistan, Bangladesh and also India are experiencing a supply disruption. Having lower LNG supplies, Far East countries have power supply issues, and in **Bangladesh or Pakistan, this is affecting the textile industry.** We have already experienced during the pandemic, that Bangladesh and Pakistan are the key producers for most of Western companies, therefore we are going to experience again a **supply disruption in the textile industry,** which is going to be translated into **higher prices and of course lower sales for Adidas, Nike,** etc. We are not shorting those stocks, but we **invested further capital into put options with maturity October 2022 at 5% OTM strike**. In addition we would like to mention, that shutting down manufactures in Bangladesh and Pakistan is going to cause again poverty, because the low salary of workers in the textile industry is the income for the whole family and governments do not have the financial capability to support unemployed citizens and their families.
- We are not starting any political discussion, but this is a part of the dilemma we were not seeing yet and it shows, the worldwide situation does not make any sense anymore. **The poorest are paying again the highest price and it is just not right.** As poorest are not only designate emerging market countries, but also lower incomers in Western countries!

LNG market and how Europe is taking supply out of poor countries

- In Europe, we are avoiding a blackout and we are increasing gas reserves in order to have enough electricity for the upcoming winter. But European lower incomers are slowly but surely not anymore in the position to live with such impressive high electricity prices.
- **In Germany for example a family face EUR 480 rise in gas bills per year. Officially, the average income in Germany is around 3'975 EUR a month, but we would assert, most of the lower incomers have to live with the half of it and 500 EUR over 2k EUR is a 25% increase not 10%.**
- As seen in the news, in UK inflation arose to 10.1% and apparently **UK retirees must start to work again, not being able to effort such high inflation.** The largest contributor was food's price and the Bank of England still expects inflation to top 13.3%
- In addition, we agree with market participants, that **the increase of the DAX index is not sustainable if energy prices in Europe are still increasing at the same pace of last few months**. Such enormous increase of costs is going to erode profit margins dramatically. The private economy is paying the full price of such situation and KTS is aware that the situation is unsustainable. Therefore we are still focusing on limiting the downside risk, because up to now, **European policy makers were not showing any magic formula, in the contrary.** As seen at page 12, productions are shutting down, causing the increase of commodity prices or supply bottleneck in certain sectors, which are translated again into a possible increase in prices for certain goods.
- **If Germany does not want to open the North Stream 2 pipeline, at least German authorities need to drastically optimize electricity consumption for public infrastructures!** We need to see more cities applying measures like the Bavarian city of Augsburg, shutting down public illumination of facades of historic building, street lights and fountains.

General news

- It is quite strange, that the **BofA Bull & Bear indicator it is still at 0,** this means at maximum bearish fro the 9th consecutive week now. But the **CNN fear & greed Index is now at 57 = greed**. We are still not at extreme greed (100 points), but the sentiment is getting a bit stretched on the short term.
- Saudi Aramco said, if required by the government, it is ready to **ramp up oil's production to its maximum capacity of 12 millilon barrels per day (bpd).** According to Bloomberg, Saudi production at the end of July was at 10.78 m bpd and the capacity has being raised to 12 mio. The company also just announced their Q2 result, reaching a record profit of USD 48.4 bn vs 25.5 in Q2 2021. With soft Chinese economic data and lower risk premium related to the war in Ukraine, the oil price dropped below USD 95, which is helping to reduce inflation's pressure. **KTS still stay invested into the energy sector**, because the oil price is going to trade sideway at those high levels and therefore the energy sector is going to reach tremendous profits and an incredible amount of cash flows. In addition, we would like to mention, that our energy's expert is invested into companies, which are in a transition phase, improving their ESG rating, which going to be translated into higher valuation' multiples. The situation in the energy sector is now similar to gold miners, which are reaching attractive cash flows with the gold price stable at 1'800 USD and valuations are extremely attractive. In addition, also gold miners are starting to increase dividend and share buyback programs.
- The Saudi billionaire Prince Alwaleed Bin Talal invested according news in Bloomberg more than USD 500 million in Russian firms: Gazprom, Lukoil, Rosneft, around the time of Moscow's invasion of Ukraine. The Saudi Wealth Fund also have a stake of USD 1.5 billion into the investment arm of the Prince. Russia and Saudi Arabia are both members of the OPEC+ , which is trying to manage oil's supply in order to help taking down global inflation.

High frequency trading (HFT)

- Mr. Schwarz posted in his blog an analysis over 85k trades placed by 6 different brokers like TD Ameritrade, E-Trade of MS, Fidelity, Robinhood and Interactive Brokers.
- The **execution's difference amongst them is up to 0.46% per trade**, no matter the size of the trade.
- This is amazing, and as explained in the book of **Michael Lewis, Flash boys** (mentioned last year in our weekly reports), companies like **Citadel, Virtu Financial** and many others, are reaching billion of USD in profits by only trading with machine learning, AI and algorithms, with **high frequency trading**, as front running stock exchange orders of investors.
- Our experts of machine learning, the team of the company Z22 in Zug, mentioned to us already long time ago, that still nowadays investment bankers are reaching tremendous profits with HFT under daylight and fully legally.
- As explained in the Micheal Lewis' book, the SEC and authorities around the globe believe the "illusion" that such high-frequency tradings are generating volume and therefore liquidity for equity markets, which is important, especially during market' corrections!
- Meanwhile normal investors are rip off in extra costs for trading. The the most "perverted" part of the medal is the fact, that high-frequency trading companies are reach such incredible profits on the huge trading volume from pension plans, therefore we can assert, that the **final "looser" of such trading activities is again the normal citizen.**
- **This is a very important duty for KTS to make sure, that stock exchange and forex orders from our clients are executed at the best price, especially in case of substantial sizes.**

Macro and general news China

- The Chinese central bank, PBOC, unexpectedly cut the rate on 1-year medium term lending facility (MLF) loans by 10 pbts to 2.75% and injected CNY 2 billion liquidity and therefore market participants are speculating, there is a liquidity issue in the Chinese financial system. In addition regulators have instructed the **state-owned China Bond Insurance Company to provide guarantees for onshore bond issuance by a few private property developers**. China Bond Insurance Co "will provide full amount, unconditional and irrecoverable joint liability guarantee". This fact shows, how the situation is serious and how Chinese authorities are working only with selected companies in order to support the real estate sector.
- Apparently the **general weakness is due to more lockdown measures and with the weakness in loan demand due to the stalling housing market.** Retail sales, industrial output and investments all slowed and missed economists estimates in July. Even the jobless rate for young people aged 16-24 climbed to 19.9% at record high, giving headache for the Communist Party.
- Mr. Excell also shows the **strong correlation between the price of Chinese real estate and consumer confidence,** which are currently both falling. This correlation was also explained by the manager of our best in class emerging market fund, Stonehorn. Chinese people believe to be wealthier, if real estate prices are rising and therefore feel more comfortable to spend money, and vice versa.

Macro and general news China

- This PBOC' measures are the proof that the normalization process is still long and the Chinese economy is still not stable enough and such negative news could definitely have repercussion on the global economy.
- Meanwhile the **NDRC (National Development and Reform Commission) said that China will boost economic demand in a strong, reasonable and moderate manner, and would accelerate infrastructure construction in Q3.** Premier Li Keqiang asked local authorities from 6 key provinces, that account for about 40% of the economy, to bolster growth. He encouraged local governments to issue debt up to the limit allowed by law, which Bloomberg says would add another CNY 1.5 trn (USD 221 bn) of debt this year to support infrastructure spending.
- A very positive news on China is the fact, that **South Korea, even USA and Germany increased direct investment into China in the last 12 months** (+37%, 26% and 14% respectively). This is coming as a big surprise, especially after the pandemic, where global companies were announcing to shift production away from China and that globalization would be dead.
- Another positive news, also already mentioned recently, is the fact, that the China's PPI (producer price index) collapsed during last 2 months. According to **historical correlation between the Chinese PPI and US CPI, inflation in USA going also to collapse, having China basically exporting deflation again.**
- As explained on the first slides, technically a lot of negative news are already discounted, but unfortunately we are still not on the "safe side" from a fundamentals perspective. We have to closely monitor various developments and still focus to limit the downside risk with trading the position QQQ and investing into put options. **Having the volatility still at attractive levels, KTS bought additional puts, at 5% OTM strike, with maturity October 2022.**

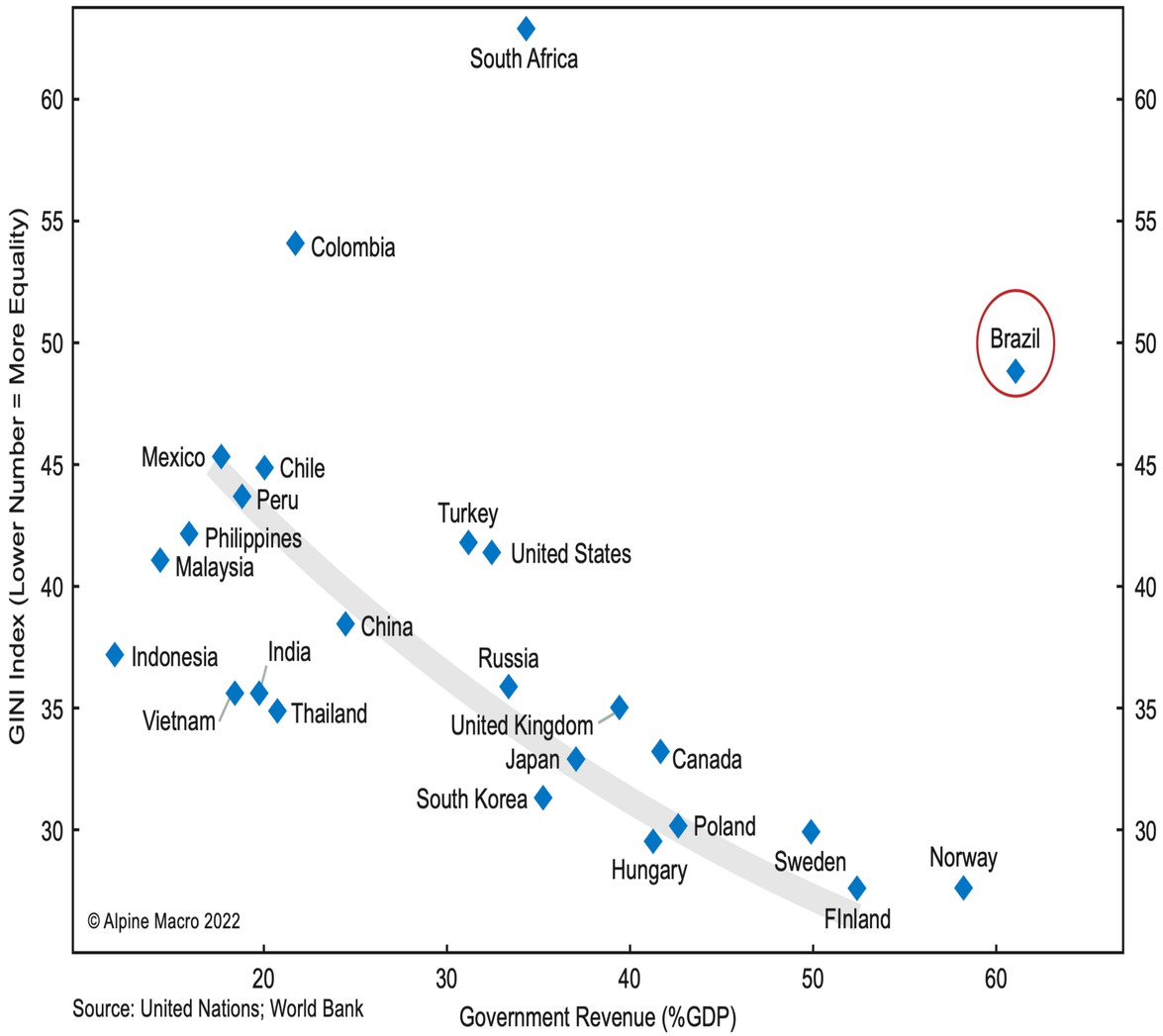
Military drills “Vostok”

- Reading that China and Russia are stepping up their cooperation, including military and **Beijing has announced sending troops to East Russia,** near the Chinese border (Vostok from the 30.8 to 5.9 drills), for joint drills at the end of the month, the first of its kind since 2018 is definitely not helping to reduce geopolitical tensions, in the contrary.
- Of course, officially there is no connection with the current international and regional situation, according to the Chinese Defense Ministry. In addition, **India, Belarus and Tajikistan are also participating** with the objective of deepening co-operation practical and friendly operation with the armies of the participating countries, improve the level of strategic collaboration and strengthen the ability to respond to various security threats.
- Journalists are arguing, that first of all, the group of countries executing the drills are representing 50% of the world’s population. Secondly such drills are a direct attack to the peace in the world.

Brazil

- On the 2nd October 2022 Brazil is going to elect their new president.
- The actual President, Mr. Jair Bolsonaro, is in a tight race with the left-wing former President Luiz Inacio Lula da Silva. **According to pools, Mr. Lula is leading with 40% vs 35%.**
- How it is possible, that Mr. Lula can run again for president? The right-hand chart is quite a perfect explanation to the question: **the public sector is extremely wasteful. Brazil's government revenues accounts for over 60% of GDP, among the highest in the world, but poorly spent, considering Brazil's extreme wealth disparity and heightened social tensions.**
- Therefore tax and public sector reforms are actually imperative, but the social system is strongly established since years now and therefore for the socialists, the only solution is Mr. Lula in order to stop reforms of Mr. Bolsonaro.

Chart 7 Tax And Social Inequality: Brazil As An Outlier



Brazilian public sector is bloated and extremely wasteful (Alpinemacro)

Brazil

- AlpineMacro issued an interesting report on Brazil and is rightly pointing out that **Mr. Bolsonaro could fix many unsolved issues over years** and therefore could hold what he promised during elections; but Bolsonaro's presidency has taken place during a highly inopportune period, as the Brazilian economy has been hit by multiple external stagflationary shocks. The CIO of AlpineMacro continues by saying that the poor handling of the Covid-19 crisis at the onset of the pandemic, strained relationships with other political forces and institutions and some other personal controversies, have all take a heavy toll on his approval rating.
- But Mr. Bolsonaro **could fix public finances.** He was able to reform the country's pension system during his first year in office. This eases an unsustainably costly fiscal burden, even though the benefit will take years to realize. In addition, Bolsonaro's administration could return to a primary surplus, after a massive Covid-induce fiscal stimulus program and a sharp spike in public debt, the country's fiscal deficit has narrowed significantly and the **debt-to-GDP ratio is on track to ease back to pre-Covid levels.**
- **Lower public debt is good for bondholders and our best-in-class emerging market debt fund is invested in Brazilian bonds.**
- The reduction in public sector could help to improve overall savings rate.
- Mr. Bolsonaro could take systematic steps to **amend legislation to reduce bureaucracy, promote entrepreneurship and attract foreign investments and therefore reaching the promised deregulation and privatization.**
- The CIO of AlpineMacro asserts, that overall, those efforts have enhanced Brazil's business environment. **The country's economic freedom parameters have improved, especially on licensing and labor restrictions, resulting an explosive growth of venture deals in recent years.**

Brazil

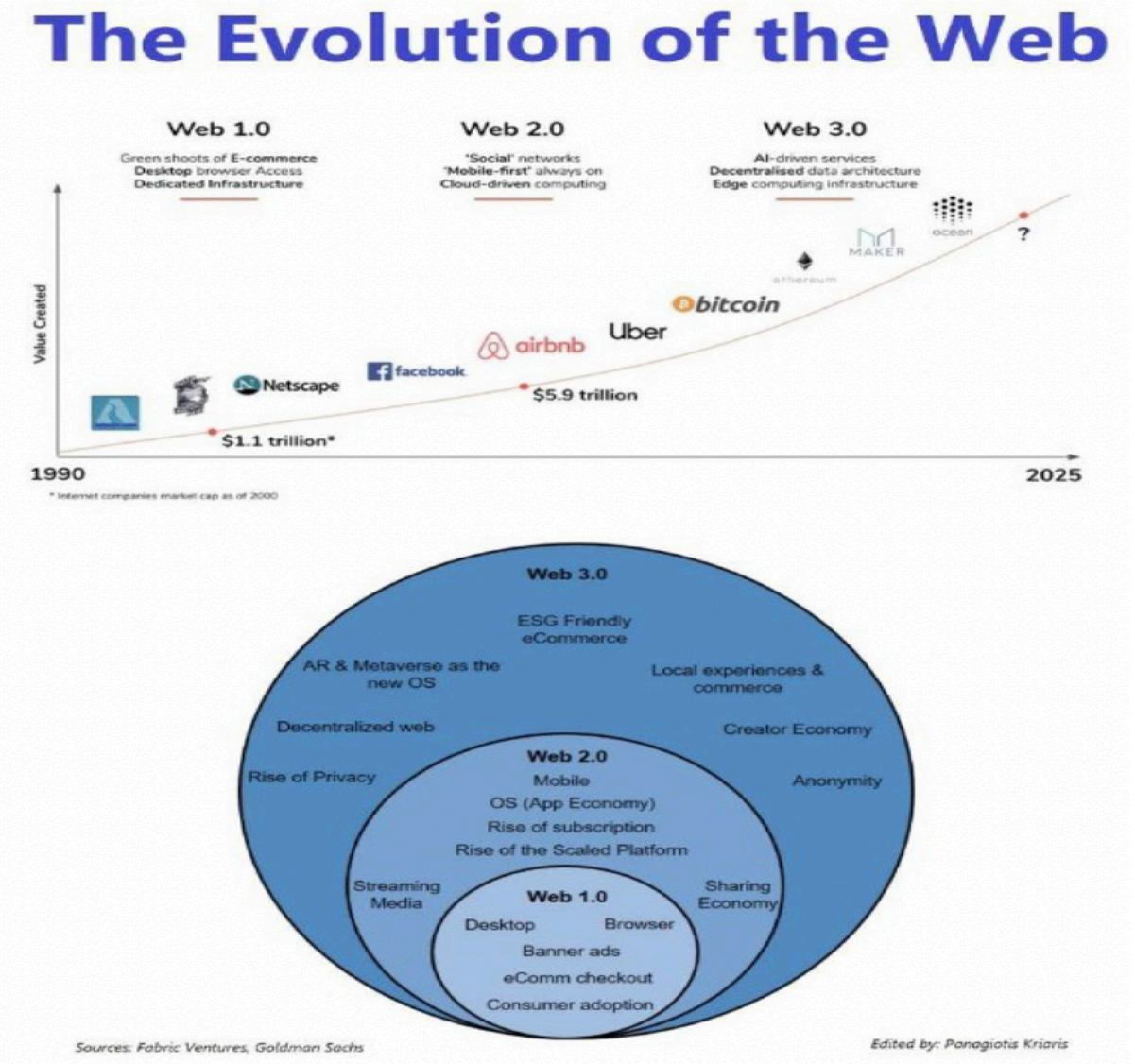
- Finally, improving institutional strength, where for example, the **central bank has been legally granted autonomy,** reducing the odds of political interference on the country's monetary policy. With its independent legal status and its single mandate to maintain price stability, the Brazilian central bank has been amongst the most aggressive major central banks in term of monetary tightening, to tame post-Covid inflationary pressures.
- The CIO concludes by saying that, in short, **President Bolsonaro has tackled some of Brazil's long-term challenges with visible positive results**. Needless to say, that enormous growth difficulties during the pandemic and Bolsonaro's populist instincts have floundered many important structural reforms that the country badly needs. The CIO also rightly assesses, that it is impossible to address all the structural problems in just 4 years.
- In the future following issues need to be addressed:
  - The **public sector is bloated and extremely wasteful.** Brazil's government revenues, including contributions and grants, accounts for over 60% of GDP, amongst the highest in the world. This crowds out the private sector and is poorly spent considering Brazil's extreme wealth disparity and hightened social tensions. Tax and public reforms are imperative. Mr. Bolsonaro is going to handle in the next 4 years and that is the biggest dilemma for socialists.
  - Brazil continues to suffer from **poor productivity and de-industrialization.** The industrial sector has continued to shrink as a share of the economy, and the export sector remains dominated by primary goods.
  - Brazil's **savings rate,** albeit having increased in recent years, **is still among the lowest in major countries**, and the pace of capital stock accumulation remains far too slow, **hindering productivity and competitiveness.**

Brazil

- The **financial system remains far too inefficient.** Interest rates amongst banks are prohibitively high for businesses and households. Currently, **real borrowing costs are at a staggering 16% compared with about 1.5% real GDP growth,** likely due to a lack of competition in the banking sector. The good news is that, real interest rates have declined substantially compared with a few years ago, and **there has been a growing fintech sector in recent years offering business and consumer loans.** Analyzing the Q2 result of the Brazilian Fintech Nubank, we have to admit that the company has experienced a tremendous growth. The company has now 65.3 million customers (+57% Y-o-Y), which means 36% of the adult population and 11% market share. The start up has USD 13.3 billion worth of deposits and reached USD 1.2 bn in revenues. The average customer is using nearly 4 products: 4 million personal loans, 700k insurance policies, 5 mio investment customers and 1 mio crypto customers.
- **As everywhere in the world now, blockchain technologies will allow Fintechs to enter such high competitiveness barriers and should help consumers to reach efficient services.** Nubank is a good example.
- Finally, according to AlpineMacro, the Brazilian economy is set to enter a period of disinflation, where growth is slow, but a major recession should be avoided.
- In Brazil, domestic mobility has already surpassed pre-pandemic levels and even **international passenger arrivals have recovered substantially, outpacing many emerging market peers, especially in Asia.**
- The labor market also has been improving.
- **The Brazilian real is modestly undervalued in real effective terms according to the Alpinemacro model. Brazilian bonds are amongst the highest yielders in emerging market both in real and nominal terms. Finally, Brazilian stocks are cheap, trading at 6 and 5.2x forward and trailing earnings respectively, both of which are near record lows.**

Web 3.0

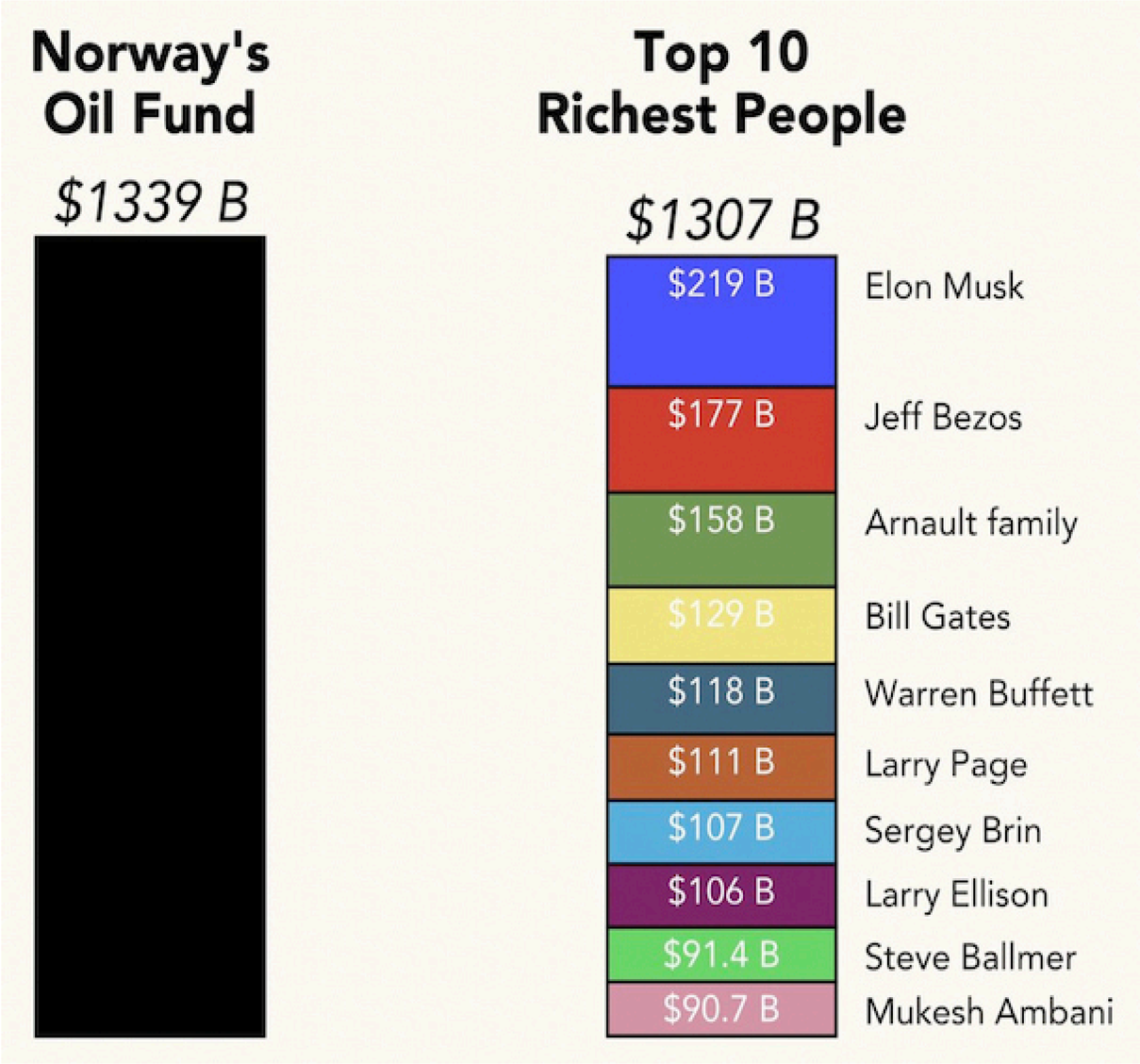
- We include in our weekly report this simple graphic, which is helping to give an idea of the evolution of the Web and in which direction the internet is going, as well the magnitude of the evolution, which is going to have a tremendous impact in our life the next decade.
- KTS believes to be well positioned into **Fintech venture capitals** in order to catch the upside potential of the segment.



Source: Syz Group

Norway’s Oil Fund

- On the right-hand chart we can notice, that the **Norway’s Oil Fund, the country’s sovereign wealth fund, is larger than the combined wealth of the richest 10 people in the world** and therefore has substantial influence into the modern financial world.
- According to Statista.com, the second biggest sovereign wealth fund worldwide is the China Investment Corporation with USD 1.22 Tn, followed by the State administration of Foreign Exchanges China with USD 980 bn.
- Abu Dhabi Investment Authority has USD 829 bn AuM.
- The government of Singapore investment Corporation owns a global portfolio of USD 799 billion, of which Temasek USD 381 bn.
- Kuwait Investment Authority owns USD 693 bn and the Public investment fund of Saudi Arabia has USD 620 billion AuM.



Source: Norges Bank (@rubenbmathisen) via Syz Group

New technology vehicle-to-grid (V2G)

- On one side we are reading in multiple sources, that Lithium's supply shortage could be a tremendous challenge in the future, on the other side we are also reading positive news, like the **vehicle-to-grid (V2G) concept.**
- According to google's description, the **V2G technology is a smart charging technology, that allows car batteries to give back to the power grid.** In essence, it treats those high-capacity batteries as not only tools to power EVs but backup storage cells for the electrical grid and this should help to avoid in the blackouts, having EV giving back electricity to the grid during time windows of peak electricity' consumption.
- We are also reading on the blog "Battery Industry", that researchers at Worcester Polytechnic Institute (WPI) have developed a **sustainable lithium recovery process, which can selectively leach and recover lithium** with formic acid before recycling valuable metals. With their method, lithium can be 99.8% recovered from layered oxide cathode materials with 99.99% purity.
- KTS believes that the EV segment is still at the beginning and of course there is a lot of skepticism. But having now all the industries and authorities going in the same direction, we believe that innovation is going to experience a tremendous development and also give new investment opportunities and for this reason we are looking with optimism to the future.

Major companies into blockchain technologies

- The right-hand chart, courtesy Mr. Aries V., Is a good summary of how major players are entering the crypto segment.
- Meanwhile the CME is going to launch Ether options on September 12, just before the Ethereum merge on the 15th of September. Market participants are therefore bullish on ether.
- KTS is not long crypto currencies.

COMPANY	SIZE OF FUNDING ROUNDS AS A PROXY OF INVESTMENT	# OF ROUNDS	BLOCKCHAIN COMPANIES INVESTED IN
Alphabet	$1,506M	4	Fireblocks, Dapper Labs, VOLTAGE, DIGITAL CURRENCY GROUP
BlackRock	$1,170.7M	3	CIRCLE, FTX, ANCHORAGE DIGITAL
Morgan Stanley	$1,110M	2	Figment, NYDIG
SAMSUNG	$979.26M	13	Flowcarbon, SAGA (SAGA.xyz), DANK BANK, YUGALABS, big whale Labs, Atomic Form, Myty, FanCraze, SKY MAVIS, Aleo, ramper, METRIKA, animoca BRANDS
Goldman Sachs	$698M	5	CERTIK, COINMETRICS, ELWOOD, BLOCKDAEMON, ANCHORAGE DIGITAL
BNY MELLON	$690M	3	TALOS, COINMETRICS, Fireblocks
PayPal	$650M	4	TALOS, LayerZero, TRM, ANCHORAGE DIGITAL
Microsoft	$477M	2	palm, CONSENSYS
Commonwealth Bank	$421M	4	Lygon, Xpansiv, GEMINI
prosus	$260M	2	iMMUTABLE
Tencent 腾讯	$224.5M	4	OXALIS, eternity, 秀合同 SHOWCON, iMMUTABLE
citi	$215M	6	TALOS, TRM, CONTOUR, BLOCKDAEMON, amberdata
UOB 大华银行	$204M	7	KYRO, avrynet, YIELD GUILD, assembly, ADDX, JAMBO, PLAY IT FORWARD DAO
WELLS FARGO	$165M	2	TALOS, ELLIPTIC
LG Life's Good	$129M	2	Jadu AR, THE SANDBOX
AMERICAN EXPRESS	$115M	2	TRM, abra

Source: Aries V of Crestline

Why you should invest early in life

- Mr. Tilmans posted a very good visualization over time, of the compounded interests' effect.
- The calculation is based a monthly investment of USD 250 for a 20 years old person to 60 years at a rate of return of 8% (a bit too high, but realistic over such a long period of time).
- **Young people are unfortunately not realizing the "power" of compounded interests and it is KTS's duty to teach the younger generation over long term effects in financials.**
- Links:
- **https://www.linkedin.com/posts/sjoerdtilmans_why-it-can-pay-off-to-invest-early-in-life-ugcPost-6965569858558136320-5eh2/?utm_source=linkedin_share&utm_medium=ios_app**

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