KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 41

The 14th of October 2022

The possible strong market signal of a bottom

- After slightly higher US CPI numbers, global equity markets collapsed to -3% , from a +1% during pre-market session.
- But during the day, equity markets rebounded and closed over +2% and therefore experiencing a +5% intra-day move.
- **The 13th October 2022's market rebound reminds us the 26th December 2018.** At the time KTS was waiting for the right signal in order to invest the liquidity, even if fundamentals did not improve overnight, investors started to turn positive.
- This year KTS started investing during the correction, having very attractive investment opportunities, but the market's move of yesterday is the signal of a powerful rebound, where we believe, shorties are slowly but surely not feeling comfortable to continue speculate on stronger inflation numbers going forward.
- Again, fundamentals are far from improving, in the contrary, but most probably, a lot of negativity is already discounted.
- **For traders, this is the time to try a long position, with stop loss the lows of the 13th October 2022.**

Hammer formation on the 13th October 2022, a 5% intra day rebound

US CPI

- KTS was expecting lower figures, but US CPI came slightly higher: the US inflation rate falls from 8.3% to 8.2% but core inflation rises from 6.3% to 6.6% . This is was most of investors were looking, only the headline number.
- Analyzing in details the US CPI, the **positive side is the collapse of durables goods,** which was largely anticipated by KTS, having major companies warning on **high inventories and forced to sell at substantial discount (**Walmart, Target, Nike, etc.).
- The VP bank is also arguing, that with weaker US consumer due to higher cost of living, combined with high inventories sales, price of goods should fall significantly going forward and the CIO concludes, that most of the Fed's work is done.
- **The CIO of MacroStrategy also argues, that the 3-month annualized rate is down to 2.01%, the lowest since Q2 2020 and basically at target.** This is a very good statement.
- The Swiss bank Julius Bär also comes to the conclusion, that now the risk of the FED over tightening is rising.
- Also **new and used car prices are collapsing** (see following slides).
- Energy and food are also slightly lower.
- The **only issue are still shelters/OER and airlines,** which are the main cause of the increase of the core inflation. On the OER we explained the issue on our weekly report nr 37 on the 16th September and for airlines is also clear, this year, everyone wants to go on holiday, having been 2 years locked down due to Covid measures. It is also quite understandable, that airlines, as also hotels and the entertainment sector increased prices in order to recuperate huge losses during lock downs.

US CPI

- As we can notice in the following slides, the own rents are still increasing, but **rent data from the real estate industry are suggesting that the peak of rent growth has been reached!** Mr. Berezin shows statistics of BCA research (source Zillow), where rents on new listings have already fell.
- **Mr. Yardeni also argues, after the strong equity market reversal, investors should buy the dips now.** He adds, inflation started to surge in early 2021, when excessively stimulate fiscal and monetary policies caused a demand shock for consumer durable goods and overwhelmed supply chains. Durable goods inflation soared last year, but moderated rapidly this year.
- In addition Mr. Yardeni says, the Ukraine war caused nondurable goods prices to soar earlier this year, particularly for energy and food, but energy inflation has also **moderated significantly since July, as economic growth slowed and US consumers sharply reduced their gasoline usage. Food inflation remains elevated, partly as a result of the drought in California.**
- Finally, also Mr. Yardeni argues, we know about the rent components of both the CPI and PCED, but **actual rent inflation for new leases soared late last year and early this year, but is coming down fast according to Zillow** same like Mr. Berezin).
- **Therefore we can assert, that most of financial experts are not quite align on the US CPI and everyone is very confident, CPI numbers are already substantially falling. Only FED members still do not want to recognize that!?**
- On the FED meeting, we all understood, the FED wants to stay on the “hard line”, but as we are going to analyze the situation in the bond market, where we can conclude, the FED is not in the position, to keep such “hard line” for longer.
- Meanwhile we are reading in Bloomberg the headline, that the personal financial manager of the President and Chief executive officer of the Bank of Atlanta, Mr. Raphael Bostic, made trades that ran against central bank rules. Mr. Powell opened a probe.

Macro - payroll expectations extremely negative going forward

- The September's payrolls data were up 263k , slightly higher than expectation, but **3.6% or 5.1 million below their 2019 high** and therefore market participants are asserting, that the adjustment is happening.
- **BoA credit strategist even forecast payroll growth to halve in Q4 and Q3 and even go negative in Q1 2023, where they will stay until the end of the year.**
- We do not know, how BoA is calculating their expectations, but from the feeling out of major companies, most of them are holding hiring and stopping new projects, as response to the costs volatility and uncertain times ahead.
- Reading such expectations, we would expect the FED to take a stance "wait and see", but we are still reading "aggressive" commentaries like from the NY Fed President, Mr. John Williams, who said the FED has more work to do to lower inflation and rebalance economic activity, warning that unemployment would likely rise and interest rates have to go higher than inflation, so at least 4.5% and therefore see inflation coming down significantly next year, but the economy still growing. As we can see in the next slides, we believe, the FED is not in the position to stay too hawkish for too long. Also as previously explained, during the FED meeting on last Wednesday, the FED was keeping the same hawkish tone for the moment.
- Meanwhile **mortgage applications and purchase demand for US housing are at lowest level in a decade,** back to levels 2008 and 2014.

UK pension plans - an anticipation of what could also happen in US and Europe

- KTS is reading alarming research, reporting that **UK pension funds were leveraged 4-5 times in bonds,** in order to compensate lower yields during past 6 years.
- KTS is shocked and was not expecting such behavior, especially because in the past, the financial sector already experienced hedge fund liquidations, having bond funds investing with leverage and as soon interest rates rose, they were forced to liquidate positions and finally closed the fund with substantial losses for investors.
- But the most alarming part is, what pension fund managers of the rest of the world did during the past 6 years? If we take into consideration, that for example the **US government was issuing more T-Bills due to stimulus packages, but China was buying USD 1 trillions less in the last 10 years,** without to talk about other countries, and the FED applying QE, but not for the whole amount issued, the natural question is, who was buying the gap? Most probably, the answer lays on pension funds' leverage, if we analyze, what happened in the UK. This is scaring, especially, because the **global pension fund industry is USD 40+ trillion industry** according to the blog of Mr. Peccatiello.
- Mr. Peccatiello argues, with years and years of lower rates and subdued cross-asset volatility led pension funds to make a more aggressive use of derivatives, not only for hedging purposes, but to invest in higher-yielding, but often illiquid assets, in order to generate better returns, with little cash as margin and with a low volatility environment.
- In Switzerland for example, KTS does not have the insurance company Swisslife on the radar screen, because the Swiss insurer, but is not the only one, was aggressively investing into Swiss real estates at stretched valuations (building at the prestigious Bahnhofstrasse at a yield of 2.5% net, at the time CHF yields were -1%), because they did not have any alternatives. **If real estate prices would fall 20% in Switzerland, Swisslife would most probably be insolvent. We hope the SNB is aware of that.**

UK pension plans - an anticipation of what could also happen in US and Europe

- One very important right consideration of Mr. Peccatiello is, **having higher volatility on the fixed income part of the portfolio** and with swings, which are at least 3-5x bigger than the last decade average, it is **mechanically impossible for large institutional investors to allocate capitals in riskier assets.**
- We understand market participants, which are arguing, it is not the time to be long equities or even bonds and are advising to invest only in cash USD or CHF. By the way, it is easy to advice, but it is practically impossible to apply, because most of asset managers have signed mandates from clients and therefore there are minimum range in any asset classes.
- On one hand, we can only agree, what happened in UK, is the endless proof, how the global financial system is a "fugazi", very fragile, but especially, people are sadly never learning from past mistakes!
- The investor community believes to understand market's dynamics, but it always turns out differently. In fact, we can not understand, how risk managers of UK pension funds, could allow such leverage and the **real question is now, what else other pension funds were implementing in their asset allocation in order to compensate lower bond's yields?**
- As KTS always explained in the last market outlooks, financial markets are based on a very fragile base and for this reason, it is important to base our investment process in limiting the downside risk.
- Even if our performance are negative YTD, KTS could mastered the drawdown in the fixed income part of the portfolio, a strategy, which was implemented in the last 6 years now. On the equity side, we could limit the drawdown, but not completely neutralized
- The only way to reach a positive performance YTD, would have being an 100% allocation in cash or be short any asset class, which is not realistic, when a family office or asset manager has a define mandate from the client.

UK pension plans - financial repression

- On the other hand, we full agree with the recent interview of Mr. Russell Napier (the magazine The market of NZZ) and such arguments are the base of KTS investment's outlook in the past several years.
- We refer to the fact, that Western governments are going to apply **financial repression** in order to reduce debt, which means, the high **indebtedness is going to be reduced vs GDP (not in absolute value, but in percentage to the national GDP), as the US did already after WWII, with a positive economic grow and real negative yields.**
- This is already happening and Mr. Napier is also right, when he asserts, that at the end of the day, central banks will not be independent, because governments are taking the final decision.
- Mr. Napier is also mentioning the latest stimulus package in Europe and Germany, in order to support lower incomers on the energy crisis, which by the way, was caused by governments themselves, meanwhile the ECB would like to start a QT in order to reduce inflation. KTS was also arguing in our recent weekly reports, that actions are not coordinated between policy makers and central bankers, but Mr. Napier is rightly arguing, eventually governments will have the final decision over central banks.
- **For this reason, and seeing what happened in the UK, we do not believe in the total collapse of the financial system, but central banks with governments are going to re-calibrate actions, in order to reach a certain stability.**

Solutions, global diversification

- What it means a certain stability?
- **Based on the fact, that financial repression is the only way out, FIAT money of highly indebted countries will substantially devalued in the next decades.** Therefore, only real assets and an international diversification will “save” the investor from such devaluation. **KTS does not believe the USD is the right safe haven over the decade and owing only CHF is not a long term solution**, especially, because Switzerland is depending to Europe much more than the international investor community believes. For this reason, we stubbornly **believe gold is a pillar of the asset allocation.** In the contrary, investment in crypto currencies is more a question of belief. KTS is arguing about the valuation of crypto currencies, not on the technology, which is clearly the pillar and the base for future development.
- In addition, we believe in **emerging market debt,** having countries with much better balance sheet’s solidity at still very attractive yields, than most of Western countries.
- In addition, governments are going to strongly influence the “free economy” and also “democracy” . Nowadays we all understood, also in Western countries, which were supposed to be highly democratic and with a completely free economy, after Covid19 ‘s actions, we know, it is not going to be the same anymore like in before.
- Interventions are happening more often, but is a logical consequence of past bad actions, where governments need to intervene again and again in order to recalibrate bad actions. We are now in a vicious spiral and we are not confident, is going to be better.
- Let take latest examples: governments decided for the “unthinkable”, mainly, lock downs. Central banks had to intervene in order to save the global financial system from the total collapse. Now we are experiencing high inflation, due to a normalization process out of lock downs and of course due to the huge liquidity injections by central banks.

Solutions, global diversification

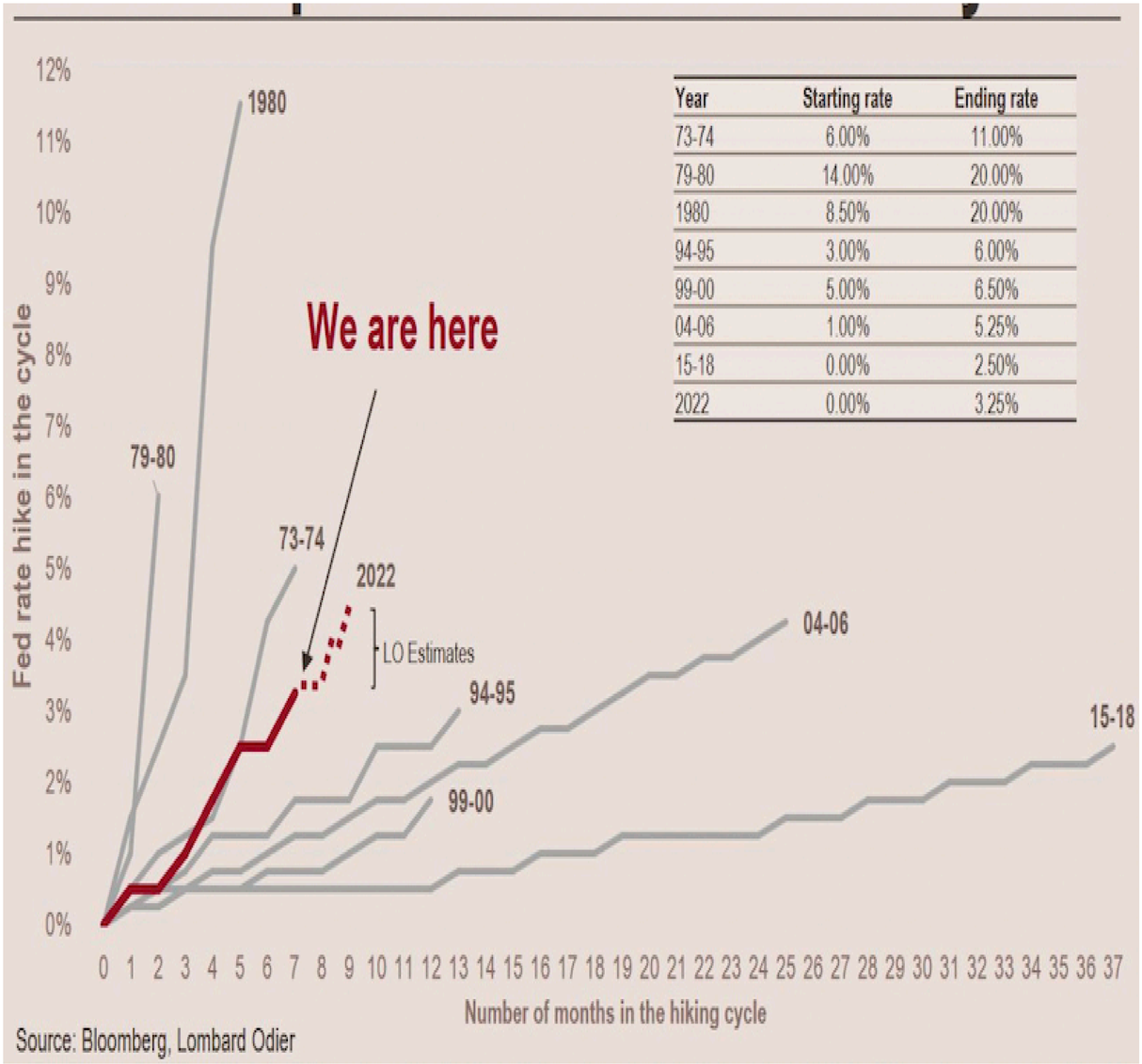
- Governments instead of looking for stability after such difficult Covid's time, initiated a war, which conduced to an energy crisis and now, especially in Europe, we need to intervene again with stimulus packages in order to support lower incomers.
- **This means higher debt,** in a time where the ECB is trying to reduce debt. The German government initiated a new EUR 200 billion energy package, but on the same time is planning to increase taxes on top German citizens, **which are moving residence elsewhere.** Having 2/3 of German income tax moving out of the country, the vicious cycle is going to start also in Germany, one of the most stable country in Europe, as it is already started long time ago in Italy, Spain, France, etc.
- **We will not be able to change such trend**. The symbolic example could be the exclamation of the German green minister, Ms. Baerbock, who said, she does not mind, what the German population wants, but her government is going to deliver weapons to Ukraine, as long Russia is not going to lose. This is said from the minister of a green party, which ideology is based on high democracy, peace in the world, save the world from pollution and no weapons ?!
- With our short but straight analysis, we want to highlight, that the financial system is not going to collapse yet, but we have to recognize long term patterns and invest or structure accordingly.
- For this reason, **we are not speculating on a total collapse of the pension fund system or bond system in the contrary,** after recent events in the UK and seeing the BoE and UK government stepping in, we believe, the FED and ECB are not in a better position, and we expect sooner than later a change in their monetary policy.
- For this reason, **we stay long equity in our mega trends and we started to take more risk also in the fixed income. After avoiding the fixed income "carnage" in our discretionary mandates,** it is time now to take some risk again.

Example on financial repressions - US debt

- We are coming across some numbers on the US debt, but the situation is quite the same in almost all the Western countries.
- With **interest rates at 3.5% and a total US debt surpassing USD 31 trillions, the annual interest expense are not over USD 1 trillion** and are surpassing social security as the largest line item in the Federal budget.
- Therefore US and the FED, but also all Western countries, are not in the position to have much higher interests rates and the FED will have to continue, as Japan is doing since 30 years now, the QE in order to compensate the missing gap.
- The **Bank of Japan's government bond holdings is exceeding 50% of the total** and it is buying in order to support the JPY and keep long-term interest rates low.
- The **FED is holding for the moment only around 20% of government bonds** and therefore there is still room for further purchase in order to keep long-term interest rates at an artificial low level.
- As we have recently mentioned, and also according a latest article in Bloomberg from the 10th October 2022 entitled **"the most powerful buyers in US Treasuries are all bailing at once"**, the whole world is selling US T-Bills, in order to support their own currencies and bonds. From Japanese pension and life insures to foreign government and US commercial banks, which once were all lining up to get their hands on US government debt, most have now stepped away, so the article. In addition to the FED, which **started the QT and plans to offload Treasuries from its balance sheet to USD 60 billion a month.** KTS believes, it is not going to work, and the FED has to step in sooner or later, like BoE and BoJ had to.
- The positive side of such spiral, is the fact, that interest rates are paid basically back to the government (FED is receiving the coupon payments) and therefore is a technical debt restructuring, which is translate in lower government debt.

All time speed of FED rate-hike cycles

- On the right-hand chart we can analyze the actual rate-hike cycles vs historical cycles.
- The actual cycles is one of the fastest of all times and the magnitude is also in line with 1973-1974.
- As explained several times, we can not compare the actual cycle with this of the 80' , when FED Chairman Volcker rose rates by 11.5% over 6 months, because of the **much higher indebtedness of the US government (31% debt vs GDP and today over 125%).**
- For this reason, we believe in the peak of FED rate hikes' expectations, which should be sooner than later positive for equity markets.
- Being a equity market rebound mostly based on lower interest rates, we believe, growth stocks are the right "bet" and therefore we are investing into the QQQ US etf.
- In addition, lower interest rates, would mean higher bond prices and for this reason, we bought some high yields bonds.

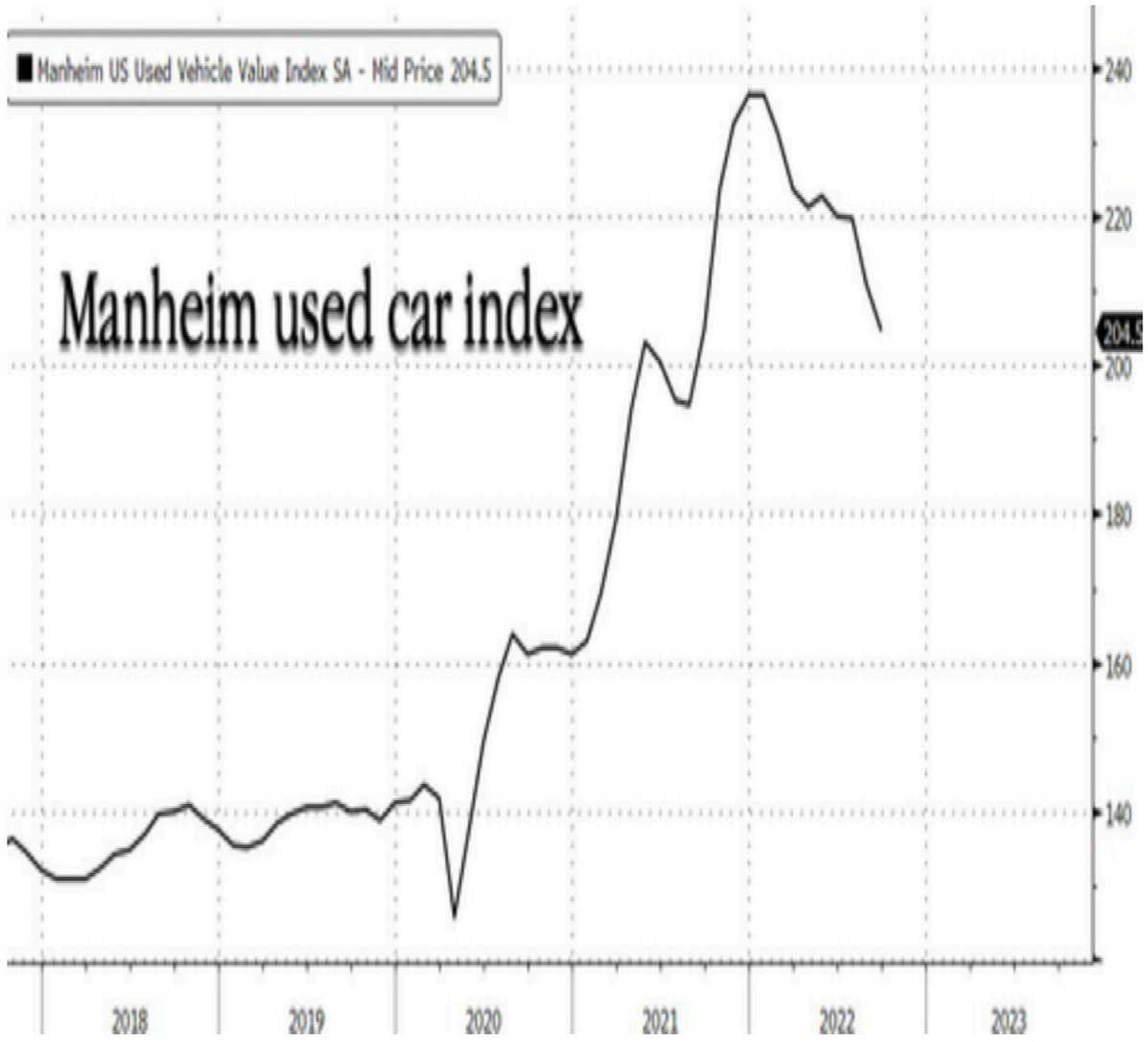


Year	Starting rate	Ending rate
73-74	6.00%	11.00%
79-80	14.00%	20.00%
1980	8.50%	20.00%
94-95	3.00%	6.00%
99-00	5.00%	6.50%
04-06	1.00%	5.25%
15-18	0.00%	2.50%
2022	0.00%	3.25%

Source: Lombard Odier

Inflation contributors - Manheim used car index constantly falling

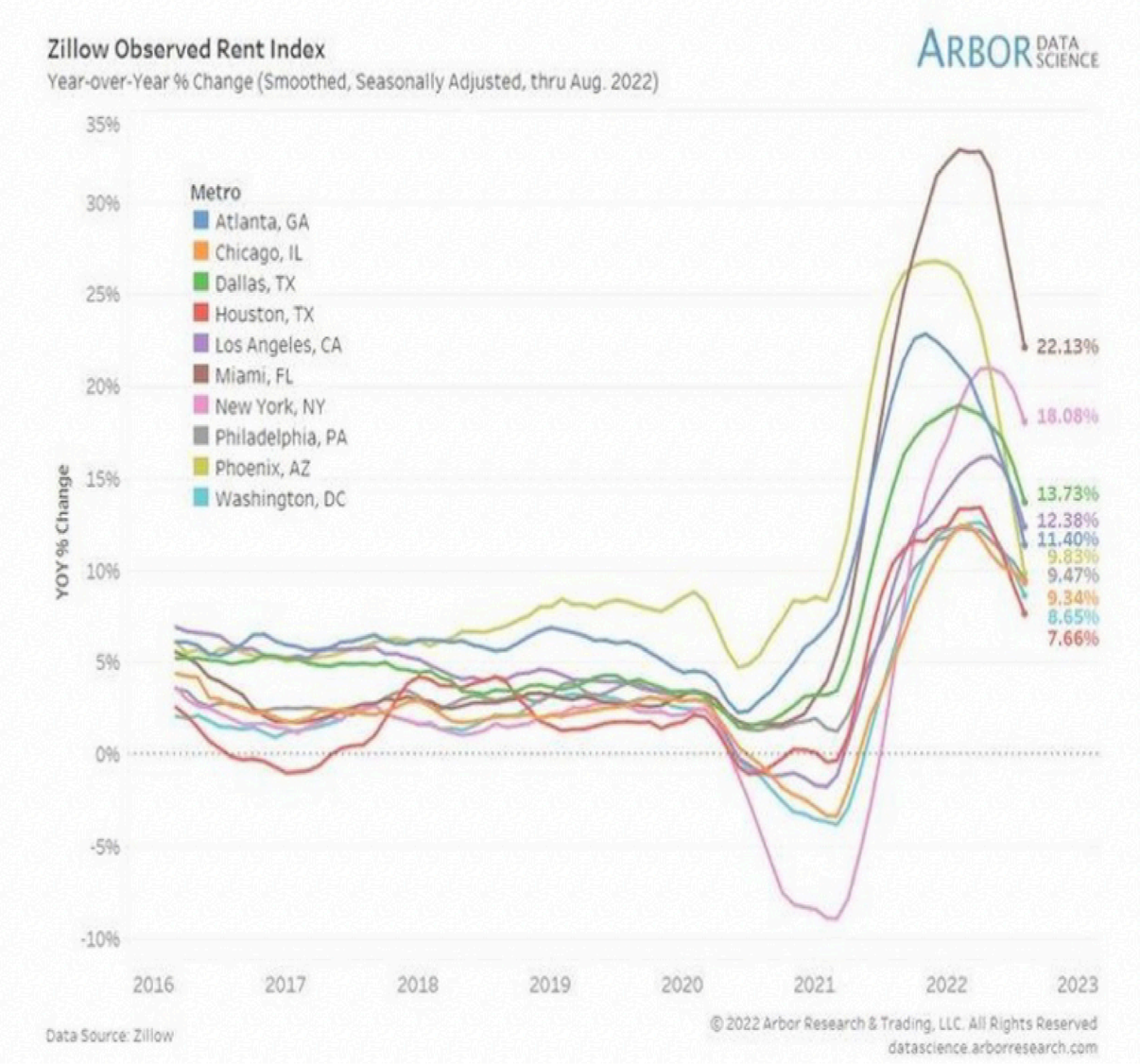
- KTS believes, inflations has peaked and we are going to analyze again the main contributors.
- As we were recently analyzing, the **used car index is constantly falling. In September the Manheim's wholesale used-vehicle prices fell 3% .**
- The index declined to 204.5 and is now finally down 0.1% from a year ago, therefore is the first annual drop since May 2020.
- Though, the index is still very high from 2020 and as we have seen, we are not sure, if prices would fall too fast, if the whole leasing sector would create major issues of increasing default ratios by banks.
- Factors, which are influencing the falling ratio of car's purchase are the higher interest rates and gas prices, which are curbing the demand.
- If we take a **linear constant increase on prices for used cars, the average would be a Index at 144,** therefore from 204.5, it is still a 30% fall.



Source: Zerohedge

Inflation contributors - rent in US falling

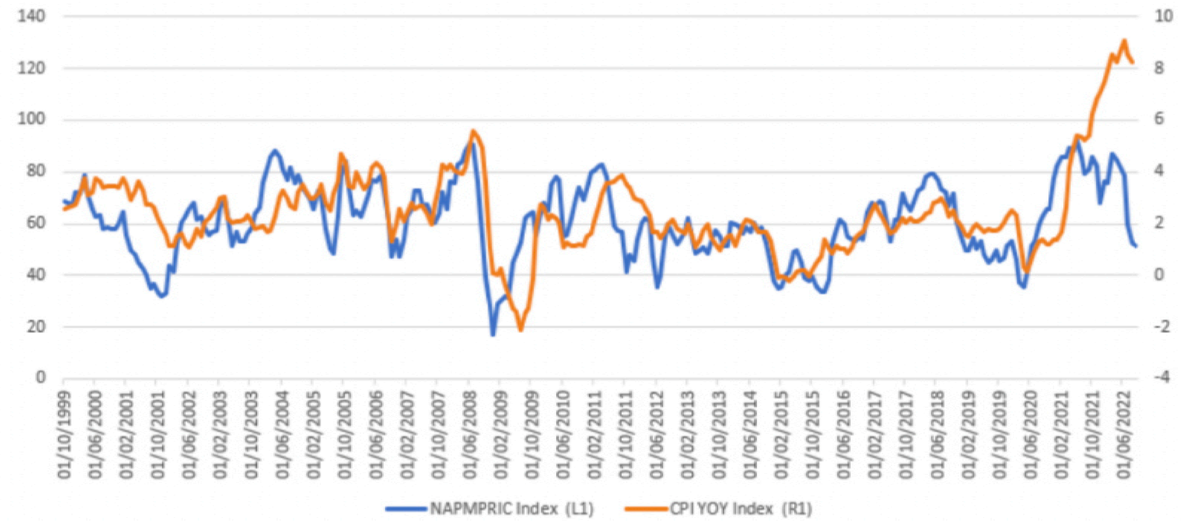
- According to data of Arbor data science, out of major cities, Miami has the highest rent growth (y/y % change), while Houston has the lowest, but are still strong relative to pre-pandemic.
- The most important factor is, in **all the cities rents are falling**.
- According to Charlie Bilello blog, rents are down in September, as **1st decline during 2022 and the YoY% increase at lowest level since May 2021.**
- In addition home price are down 6% from the peak in June, not to talk to the plumbing home sales (-28% from peak) and mortgage applications.
- If we add, that oil is still down around 40% form the highs in March and global freight rates are down around 57% YTD, inflation as definitely peaked, but still not enough to have a FED changing to a dovish tone.
- **In the CPI number of yesterday, we still do not see this development, but shot come into next numbers.**



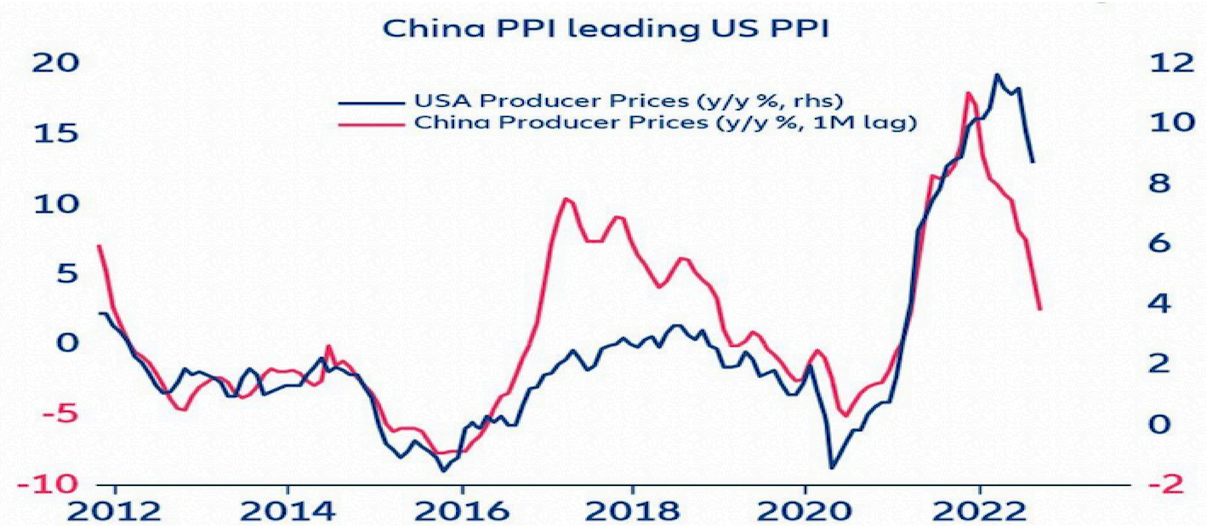
Source: Arbor Data Science via Syz Group

ISM prices paid

- According to the research Macro strategy, the **ISM prices paid is pointing to significant lower US CPI numbers going forward,** at least for goods, which are the smallest part of the CPI with 27% , but the most volatile.
- The ISM prices paid index (blue line) is falling mainly do to de-bottlenecking, not having lockdowns anymore.
- On the right-hand chart, courtesy Allianz research, we can notice, how **Chinese producer prices fell substantially and having an high correlation to US PPI, we should expect soon lower prices also in US**. Allianz research argues, China is becoming the best ally for global central banks in order to fight inflation.
- As have recently argued, Western countries were enjoying 20 years of low inflation due to globalization, having cheap energy sources from Russia and cheap goods from China.



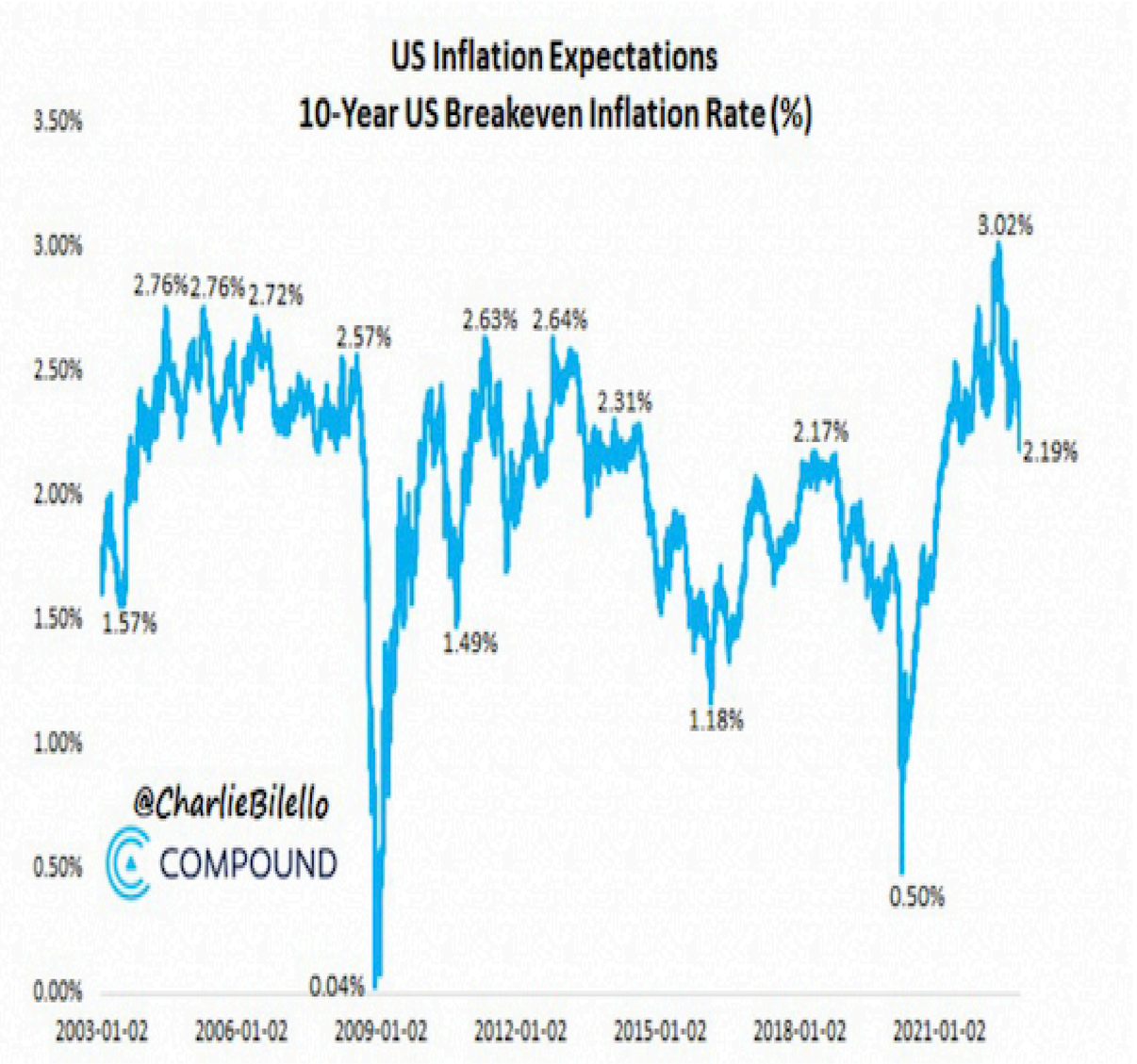
ISM prices paid (blue) vs US CPI: sooner lower CPI numbers (Macro strategy



China PPI (red) vs US PPI: soon lower PPI in US (Allianz Research)

Inflation expectations

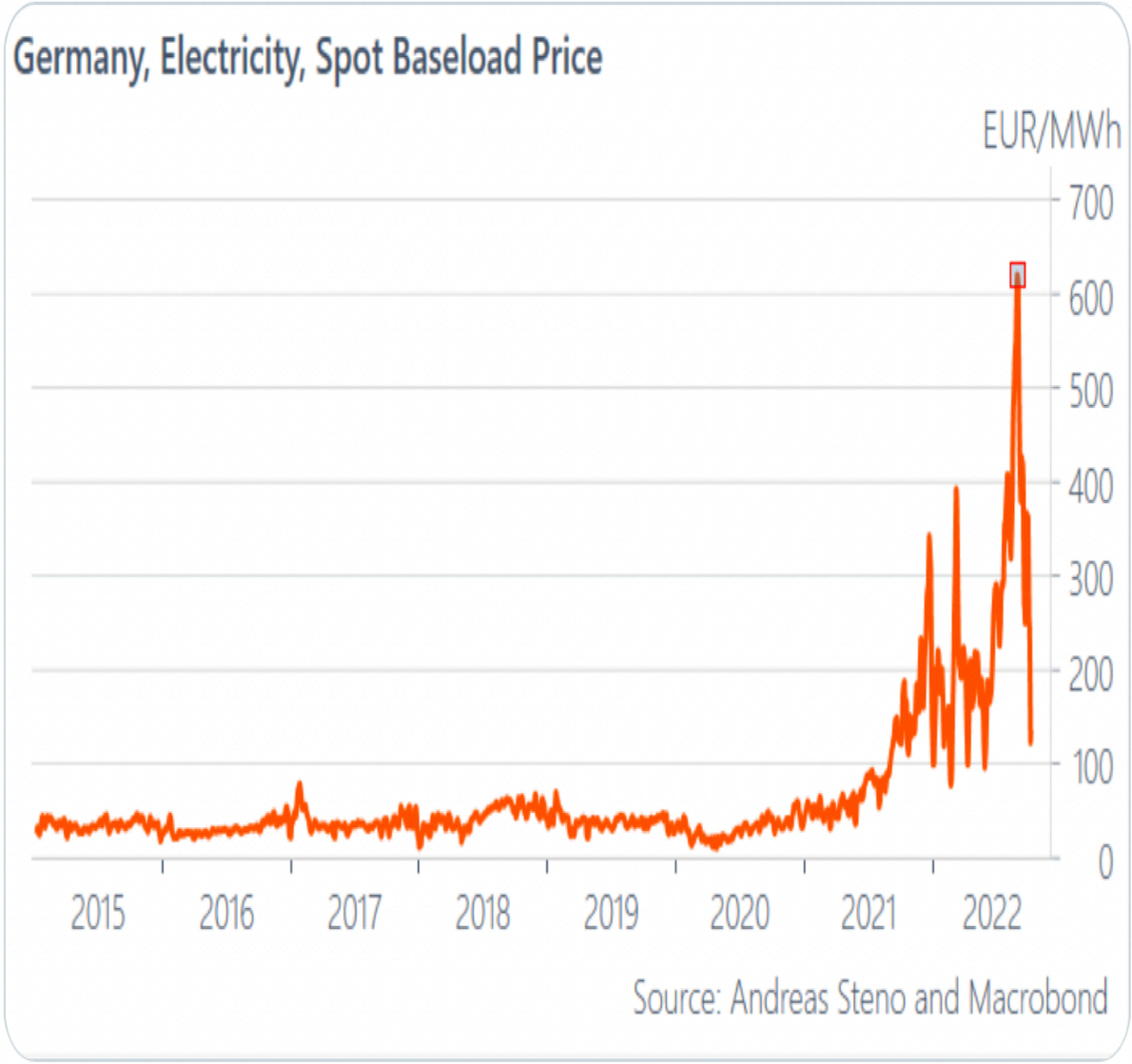
- Meanwhile **inflation's expectations over 10 year are falling to a 18-month low to 2.19%,** from a peak of 3.02% in April as a result of a global slowdown of the economy growth due to tightening monetary policies.
- As we know, inflation is by definition a lagging indicator and therefore, we need to actively analyze the index of every single contributors, in order to anticipate inflation's numbers.
- We do not have to forget, that industrial prices fell substantially. An example is the Lumber prices, which had a spike back at the beginning of the year, and today is at -70% from March high.
- Also cereal price index has fallen 16% from highs, but still +45% above its pre-pandemic range.
- The only negative variant is the oil prices, after the OPEC+ cut of 2mio barrels a day. The oil prices climbed back to 90 USD, but for the moment has not experienced any price's spike, which is positive. But market participants warn about China economy re-opening and oil shortages, as explained last week.



Source: Charlie Bilello via Syz Group

European natural gas prices collapsed

- The price of natural gas in Europe collapsed and normalized.
- From over 600 EUR / Mwh, in basically 1 month we are back to 100 EUR/Mwh.
- Having a milder-than-expected autumn combined with the fact, that gas storage in the EU is now at more than 90% and finally, EU managed to reduce its gas consumption by 10%, natural gas prices are falling, because there is no more place to storage it.
- Even Italy started to export gas again, having storage full.
- This are of course great news for Europe.



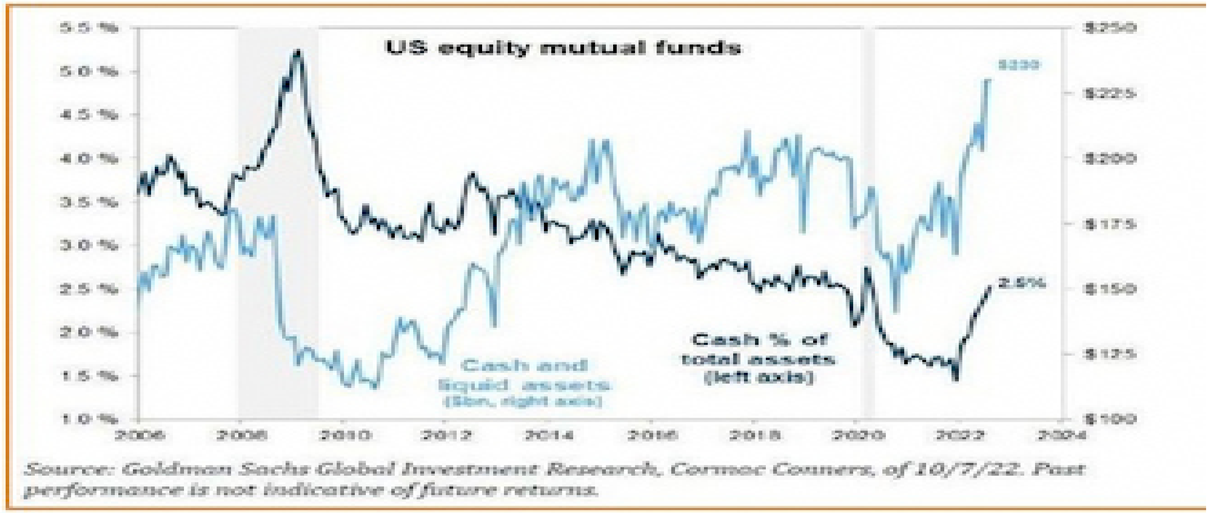
Source: Andreas StenoLarsen/Macrobond

ARK open letter to the FED

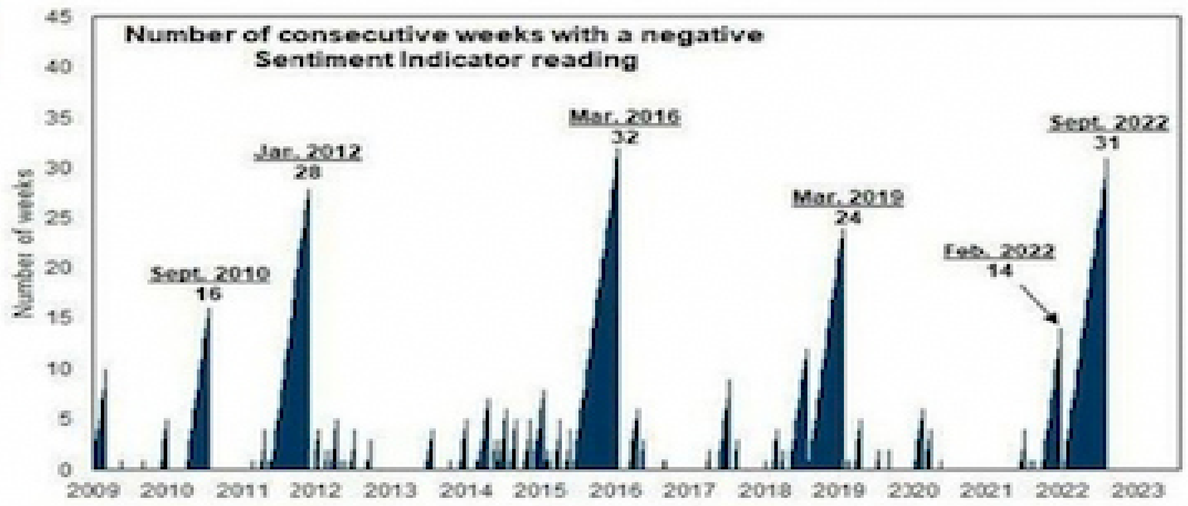
- Ms. Catherine Wood wrote an open letter to the FED, arguing, that the **FED is wrongly focusing on 2 variables (employment and headline inflation), which are lagging indicators.**
- ARK argues, that the **leading indicators to focus are commodity prices in addition to inventory accumulation**, which are already indicating a deflationary environment.
- ARK also adds, that the **FED should not fight again food and energy inflation, which are a consequence of the Ukraine conflict** due to supply shock to agriculture and energy commodities.
- In the letter is explained, how inventory accumulation seems to be overwhelming manufacturers and retailers. As KTS recently argued, we are already experiencing the **"bullwhip" effect, as per news of Walmart, Target and Nike and of course used cars.**
- Many market participants see the letter as a sign of desperation, but KTS is of the opinion, that the remarks done by Cathy Wood & team are reflexing reality and therefore we find the inputs valuable.
- Mr. Michael Burry says about Ark ETF: " How anyone over the age of 40 did not see it coming is a riddle. The answer is Greed". Back in February 2021 KTS was arguing that valuations of many start ups, meme stocks or non-profitable companies were insane and sooner valuations would fall back to reality. This has being the case, having the **Ark ETF falling 77% from highs.** But nowadays we have to admit, there are in the market valuable companies with solid business, strong balance sheet and attractive growth, which are actually a "screaming buy", as it was a "screaming sell" back in February 2021.
- To the links of the ARK's letter: https://ark-invest.com/articles/market-commentary/open-letter-to-the-fed/

Signs of capitulation - highest cash level, volume puts, negative weeks

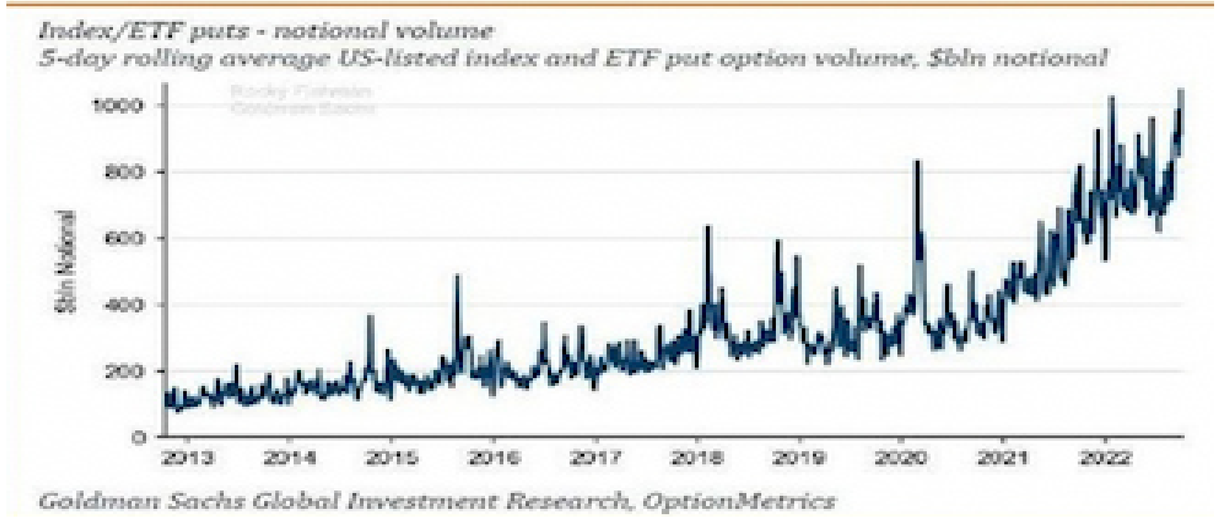
- According to Goldman Sachs trading desk, information via Syz group, we are seeing signs of capitulation by retail investors.
- **First Mutual Fund cash levels is at all-time highs**
- The 5-day rolling average notional of index puts is USD 1 trillion, per day, every day, that's a new record and the significant negative price action on the Friday 7th October was mostly due to aggressive hedging pressure (gamma covering).
- GS sentiment indicator is now negative for **31 straight weeks**, the second longest streak on record (max was 32w in 2016).



Highest Cash levels ever by US equity mutual funds



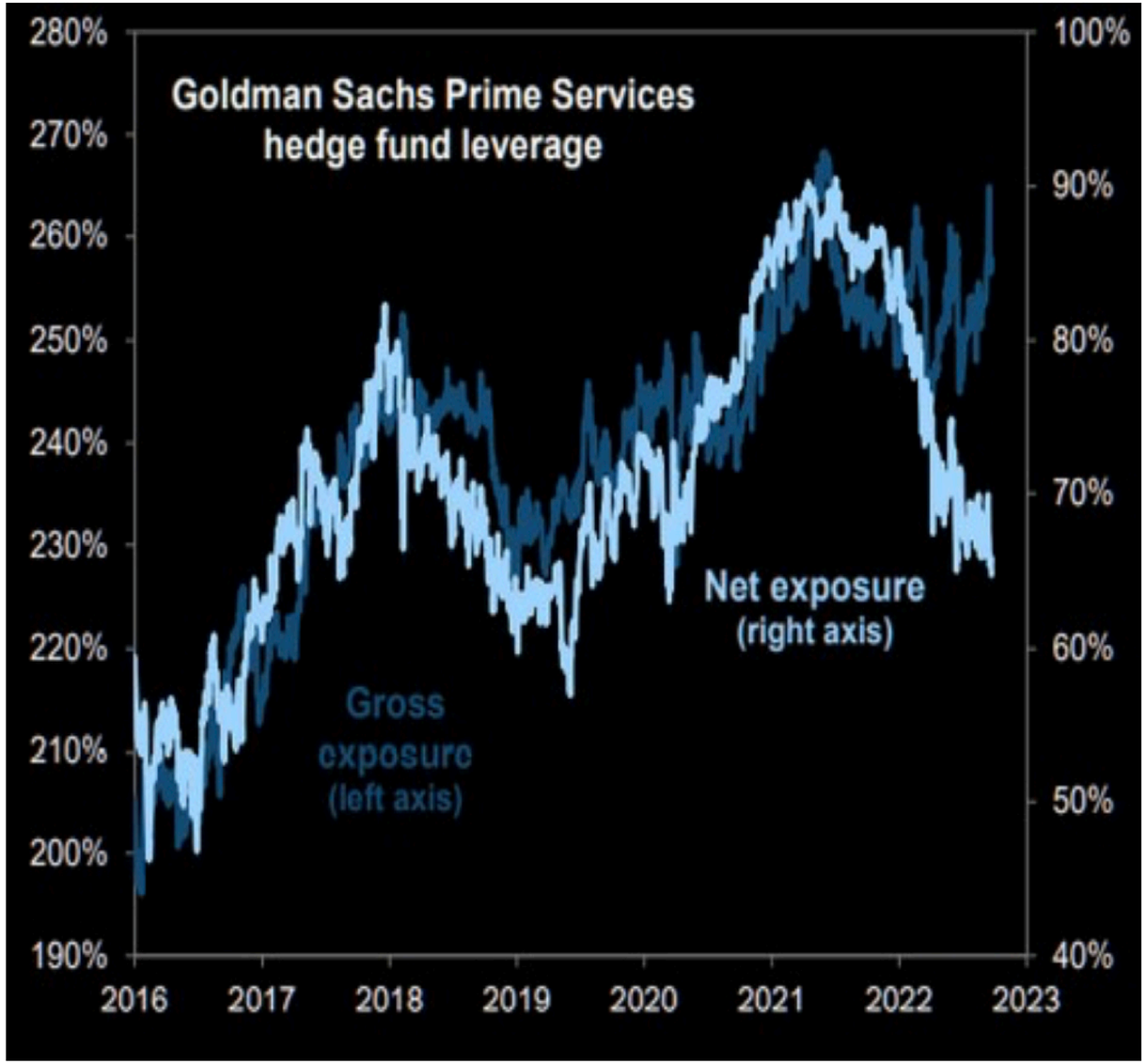
31 straight negative weeks, vs record 32 weeks in March 2016



Highest put volume ever (investors are not selling, but hedging with puts)

Signs of capitulation - gross leverage by hedge funds at lowest levels

- According to Goldman Sachs, Hedge funds had a very low net exposure.
- The chart on the right-hand side is showing the gross leverage among hedge funds has been going up, but the net leverage has been going down. What does this mean?
- According to investingwhisperer, it means, funds are getting more leveraged but also less long stocks.
- **The gross exposure is as high as February 2021, but back then, funds were very long equity, this time funds are leveraged up and short, or at least a lot more short then they have been in a very long time. Having US CPI not that bad, some HF closed short positions.**
- This time, funds are bearish, but with pair trades, keeping long positions (most probably defensive and high dividend yields) and adding to their shorts.



Source: Goldman Sachs

Signs of capitulation - 2nd worst year on record for portfolio 60/40

- Goldman Sachs also explains, that **since 1900, 122 years of data**, through Q3 2022, the US 60/40 “worlds and voting retirement” **Portfolio is down -21%, for the 2nd worst year on record** (1974 was the only year worse, during the last inflation spike, CPI jumped from 3.4% in 1972 to 12.3% in 1974).
- Since 1900, through Q3, the **S&P 500 Index is down -24%, therefore the 4th worst year on record** (only 1931- great depression, 1974 - inflation, 2002 - internet bubble, were worst).
- Since 1900, through Q3, **10 year US Treasuries are down -17% for the worst year on record**. 1987 was the second worse, and bonds were down -10% .
- For the first time in history, both asset classes, equity and bonds, lost over 10% (see specific slide).
- Basically Goldman Sachs is arguing, that the **retail investor is the last standing asset owner, who has not sold and is moving into money market right now. Retail added USD 89 billion worth of money market inflows last week, as we have seen in our last weekly report. Retail investors are also selling their darling single stocks like Apple and Tesla.**
- The **money market inflows of last week was the largest inflow into cash since April 8th 2020** (USD 102 billion) and also bonds had the second largest outflows since April 1st 2020 (USD 18 billion weekly outflows vs USD 27 b in 2020).
- Goldman Sachs argues, the last capitulation is going to be this week with the CPI numbers. Strange enough, this is apparently happening, if we analyze the equity market’s behavior on the 13th October, even if during today’s session, everything is put in discussion again.

Signs of capitulation - cheap valuations

- GS also argues that the current discretionary hedge is too short and they start to see first macro covering. In addition GS rightly argue, that **mutual funds will not want to show such high cash at the end of the year and therefore are going to invest in the next months**. **GS is also rightly arguing, mutual funds are going to buy the winners like energy stocks. For this reason, KTS must keep the exposure into energy stocks.**
- According to the statistic of Omnis Investment, the **longest bear market lasted in year 2000 over 3.2 years and was -46%** . The average of bear market is 0.9years and -31% . **Nowadays the S&P 500 is -24% and Nasdaq -35% .**
- **Small cap valuation are at 11x forward P/E, which is the same cheapest level since 1990 and year 2008 and according to Alpine macro, the S&P 500 P/E ratio excluding FAAMG is 12x**
- On the other hand, reading some other research, as for example of The Macro Strategy, **some investors are expecting correction of additional 20% to even 50% from nowadays levels**, based on the fact that such high inflation in the past was corrected only with recession and having had for long time a ultra accommodative monetary policy, **now with the inverse process and falling M2 liquidity, they see a fair valuation in Nasdaq by 5'000 points,** vs over 10k nowadays. KTS understand the logic behind such conclusion and analyzed several charts, showing the over proportional development of US wealth over US GDP, but we do not have to forget, that nowadays major companies have the highest levels of cash ever and therefore, it is difficult do compare the nowadays situation with past developments. For this reason, **we believe, the trust is somewhere in the middle and after such substantial correction in global wealth, we should have finally a floor.**
- Even the forever bearish, Mr. Marc Faber, is turning more optimistic on the short term and expect the lows in October for a strong rebound on the short term. Though on the longer term, we have not seen the lows yet and see even stronger correction.

Signs of capitulation - cheap valuations

- As our clients remember, during the year 2020, KTS could reach a tremendous outperformance in the Biotech sector with the outperformance of our best in class fund PMG Biotech, but especially with the clear overweight of the vaccine producer **Biontech**, which was the stock pick for the best vaccine of our biotech expert, Ms. Myoung. We have high respect for her knowledge and we would like to remind, that the main argument for such decision, was based on the fact, that not only Biontech have a better technology than Moderna & others, but **Biontech was the only company, which had 4 vaccines in trial, all the other had only 1.**
- As you know, we bought again the stock, having again governments advising for the booster against Covid and the incredible fact of the stock Biotech nowadays is, **it is trading at a 3x P/E with half of the market cap in net cash.**
- As explained, in the market there are now many extremely attractive buying opportunities.

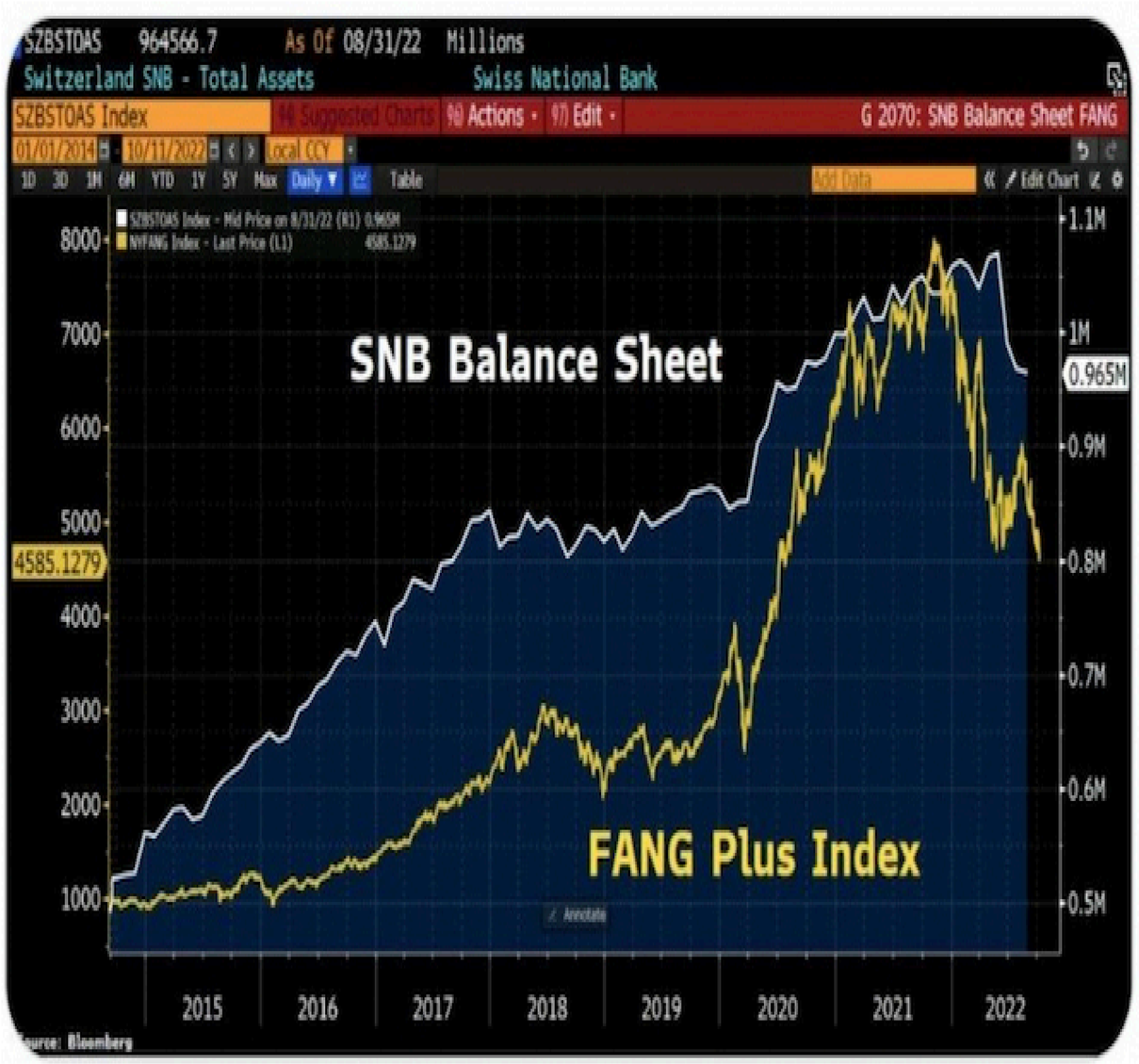
Picture Title

Additional example of cheap valuations

- TSMC, Taiwan Semicondutcor. We fully agree with the analyst of Julius Bär, whereby the company has suffered excessively from the brunt of US-China geopolitics and now is trading at 10-year lows P/E valuations, despite 2022expected EPS being 60% higher than in 2021. Even if 2023e EPS fell 20%, it would be 30% higher than 2021's EPS. The only other time in the last 15 years that earnings fell by high teens was in 2011 and therefore the analyst maintain a buy rating. This is an additional example, for KTS is hard to predict an additional correction of over 20% of equity markets, which some solid companies like TSM are trading at such multiple, generating a tremendous amount of cash flow and still growing. We do not to forget, that TSMC is producing 80% of all the high end chip worldwide and such know how is not going to disappear overnight.
- We add another incredible example: GEVO US. The stock is trading at 2 USD, substantially under the net cash position of over USD 600 mio. Gevo is not going to be cash burning like a biotech company and around USD 450 mio are going to be used as equity for building the Net Zero 1 plant (total costs around USD 850 million). The NZ1 plant is supposed to generate USD 300 mio in ebitda starting from 2025. The NPV (net present value) of future cash flows is around 8 to 10 USD. Gevo has in addition USD 600 mio in tax credit and IP (intellectual property) valued around USD 450 mio. Therefore, the value per share of cash + IP + tax losses is alone around USD 6 , in addition to additional USD 8 in NPV. Being the stock GEVO included in most of "green passive etfs", 2/3 of GEVO's shareholders are passive asset managers. Therefore, we start to seriously believe, if a major competitors would offer only USD 4, which would correspond to a 100% premium to the today's stock price, the majority of shareholders would accept the offer and the competitor would buy 11 year of hard work and proven technology basically for free.

Swiss National Bank selling FANG

- A few weeks ago we all realized, that the SNB started to sell US etfs in order to reduce the balance sheet.
- A reason of the market drawdown is in fact the QT, where central banks are not only stopping to buy bonds, but also selling equities. Apparently the FED shuttled USD 3.1 billion to the SNB to cover an emergency dollar shortfall and it was the first time, the FED sent USD to the SNB using the swap line in such size. It sounds like, the FED was in urgent need of these USD, not the SNB?
- The strong intra-day reversal of the 13th October 2022 is perhaps the indication, that for the moment such sales stopped? The BofA CIO, Mr. Michael Hartnett, said, markets stop panicking when central banks start panicking. It looks like, it is the case again here.
- Market participants like Mr. Yoon is also asserting like KTS, the final phase of the market decline is going to be caused by the blue chip stocks, which has not plunged yet and the SNB selling was helping for such final phase.



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For the first time in history, both US equities and bonds, lost over 10%

- As we recently explained, for the first time in history the diversification between bond and equity, did not work out.
- In fact, it is the first time in history, that the S&P 500 Index lost 23.4%, the 10y US Treasury -16.7% and therefore the 60/40 portfolio is YTD -21%
- According to a historical research of Lombard Odier, **US stocks vs Bonds returns from 1926 to 2022, year 2022 is the same as 1931 and 1969.** On year 1932, equity markets started to rebound only in July and a sustainable rally was only in March 1933. Meanwhile in June 1970 equity markets started a tremendous rebound.
- KTS was working over years successfully on diversifying out of plain vanilla bonds, in order **to avoid such significant drawdown on the worst bond crash in the history!.**
- But now KTS believes, there is also the positive side of the event. After such substantial drawdown in basically all the asset classes, if an investor has a 1-2 year horizon, we should finally experience positive performances.

S&P 500, US 10-Year Treasury, and 60/40 Portfolio (Total Returns, 1928 - 2022)

Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40
1928	43.8%	0.8%	26.6%	1947	5.2%	0.9%	3.5%	1966	-10.0%	2.9%	-4.8%	1985	31.2%	25.7%	29.0%	2004	10.9%	4.5%	8.2%
1929	-8.3%	4.2%	-3.3%	1948	5.7%	2.0%	4.2%	1967	23.8%	-1.6%	13.6%	1986	18.5%	24.3%	20.8%	2005	4.9%	2.9%	4.0%
1930	-25.1%	4.5%	-13.3%	1949	18.3%	4.7%	12.8%	1968	10.8%	3.3%	7.8%	1987	5.8%	-5.0%	1.5%	2006	15.8%	2.0%	10.2%
1931	-43.8%	-2.6%	-27.3%	1950	30.8%	0.4%	18.7%	1969	-8.2%	-5.0%	-7.0%	1988	16.6%	8.2%	13.2%	2007	5.5%	10.2%	7.4%
1932	-8.6%	8.8%	-1.7%	1951	23.7%	-0.3%	14.1%	1970	3.6%	16.8%	8.8%	1989	31.7%	17.7%	26.0%	2008	-37.0%	20.1%	-13.9%
1933	50.0%	1.9%	30.7%	1952	18.2%	2.3%	11.8%	1971	14.2%	9.8%	12.4%	1990	-3.1%	6.2%	0.7%	2009	26.5%	-11.1%	11.1%
1934	-1.2%	8.0%	2.5%	1953	-1.2%	4.1%	0.9%	1972	18.8%	2.8%	12.4%	1991	30.5%	15.0%	24.1%	2010	15.1%	8.5%	12.3%
1935	46.7%	4.5%	29.8%	1954	52.6%	3.3%	32.9%	1973	-14.3%	3.7%	-7.1%	1992	7.6%	9.4%	8.2%	2011	2.1%	16.0%	7.7%
1936	31.9%	5.0%	21.2%	1955	32.6%	-1.3%	19.0%	1974	-25.9%	2.0%	-14.7%	1993	10.1%	14.2%	11.7%	2012	16.0%	3.0%	10.7%
1937	-35.3%	1.4%	-20.7%	1956	7.4%	-2.3%	3.6%	1975	37.0%	3.6%	23.6%	1994	1.3%	-8.0%	-2.4%	2013	32.4%	-9.1%	15.6%
1938	29.3%	4.2%	19.3%	1957	-10.5%	6.8%	-3.6%	1976	23.8%	16.0%	20.7%	1995	37.6%	23.5%	31.7%	2014	13.7%	10.7%	12.4%
1939	-1.1%	4.4%	1.1%	1958	43.7%	-2.1%	25.4%	1977	-7.0%	1.3%	-3.7%	1996	23.0%	1.4%	14.2%	2015	1.4%	1.3%	1.3%
1940	-10.7%	5.4%	-4.2%	1959	12.1%	-2.6%	6.2%	1978	6.5%	-0.8%	3.6%	1997	33.4%	9.9%	23.8%	2016	12.0%	0.7%	7.3%
1941	-12.8%	-2.0%	-8.5%	1960	0.3%	11.6%	4.9%	1979	18.5%	0.7%	11.4%	1998	28.6%	14.9%	23.0%	2017	21.8%	2.8%	14.1%
1942	19.2%	2.3%	12.4%	1961	26.6%	2.1%	16.8%	1980	31.7%	-3.0%	17.8%	1999	21.0%	-8.3%	9.2%	2018	-4.4%	0.0%	-2.5%
1943	25.1%	2.5%	16.0%	1962	-8.8%	5.7%	-3.0%	1981	-4.7%	8.2%	0.5%	2000	-9.1%	16.7%	1.2%	2019	31.5%	9.6%	22.6%
1944	19.0%	2.6%	12.4%	1963	22.6%	1.7%	14.2%	1982	20.4%	32.8%	25.4%	2001	-11.9%	5.6%	-4.9%	2020	18.4%	11.3%	15.3%
1945	35.8%	3.8%	23.0%	1964	16.4%	3.7%	11.3%	1983	22.3%	3.2%	14.7%	2002	-22.1%	15.1%	-7.1%	2021	28.7%	-4.4%	15.3%
1946	-8.4%	3.1%	-3.8%	1965	12.4%	0.7%	7.7%	1984	6.1%	13.7%	9.2%	2003	28.7%	0.4%	17.2%	2022*	-23.9%	-16.7%	-21.0%

Source: CharliBilello via Mr. Tocchetti

Energy sector, the oil price

- As we know, the energy sector is by far the best performer YTD, with over 50% outperformance to the second best, Utilities and consumer staples.
- But more importantly, the **energy sector has an average of 11% FCF yield** according to Crescat Capital and therefore insanely cheap.
- In addition, market participants are arguing, that only **Apple with a market cap of USD 2.25 trillion is more value than all the US energy stocks in the S&P 500 Index (USD 1.77 trillion**, with the most important Exxon, followed by Chevron, ConocoPhillips). This is the reason, why we keep our exposure in the energy sector.
- Exxon market cap is now above Meta, first time since 2016.

The oil price

- Some market participants are arguing, that the OPEC+ and Wall Street are disconnected between the extremely tight physical market and the oil price.
- Experts are of the opinion, in the futures market is manipulated by the US government after the cut of the OPEC+ and has just released 7.7 million barrels of oil into the market last week.
- Therefore, the price of oil will be weak, until the physical markets regain their dominance relative to the future market. Experts speculate, this going to happen, when inventory levels get so low, that an emergency-type mentality take over in the physical market and expect chaos.
- According to the worldpopulationreview.com, US oil reserves are in fact at the lowest level since 1984, at around **450 million barrels, but should still suffice for another 5 years.** Therefore there is still enough time, because the oil market enter in a chaos, but meanwhile, a oil price not spiking is the best, what can happen for a lower inflation.
- KTS stay invested in the oil sector as hedge of geopolitical tensions and because we are entering into the tax losses period, therefore the best performers of the year are added, meanwhile the worst are sold.

General news

- According to a chart of our world in data (via Mr. Peccatiello), the **US has the highest healthcare expenditure per capita over the last 50 years, but US life expectancy is very low compared to other developed countries** and Mr. Peccatiello is rightly asking, if some of it has to do with diet, exercise and lifestyle.
- In our next weekly we will analyzed US elections. Reading initial commentaries, it appears quite clear, that Republicans should win the House.

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