KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 44

The 4th of November 2022

FED on the 2nd November 2022 - the FED actually slowing down pace

- Global central banks started changing to a dovish tone, realizing being at the edge of a total collapse of the financial system and equity markets could find a bottom, and even the FED initially was giving some hopes of more dovish tone by saying "in determining the pace of future increases in the target range, the Committee will take into account the cumulative tightening of monetary policy, the **lags with which monetary policy affects economic activity and inflation,** and economic and financial developments", letting investors believe in a possible policy change, whereby we will have more increases but possibly smaller. But during his speech, **Mr. Powell went on with a more hawkish tone**, by saying:
  - The incoming data since our last meeting (labor and CPI) suggest the **terminal rate of FED funds will be higher than previously expected (4.63%) and we will stay the course until the job is done.** Some investors are forecasting 5% for 2023 and lining out dramatic economic scenario. KTS believes, 5% is not possible, because the global economy is already deteriorating at a fast speed and the FED will have to change policy soon.
  - **If we were to over-tighten, we could use our tools to support the economy later on**, from a risk management perspective, that's a better risk to run than to underdeliver on tightening and risk inflation getting entrenched.
  - On the stock markets rallying, Mr. Powell answered: "We have ways to go when it comes to raising interest rates, and we will **ensure financial conditions are tight enough to bring economic activity and inflation down".**
- Mr. Peccatiello argues, this is as hawkish as it gets, the pivot of the **FED is from hawkish to more hawkish** and stock markets reacted negatively on the 2nd and 3rd of November.
- Other market participants are arguing that the **FED pivot is going to be when the economy is going to collapse and therefore, equity markets will not have any rally soon.**

FED on the 2nd November 2022 - the FED will hike buy at smaller steps

- But the main message to take is also the fact that, bottom line, the **front loading in rate hikes is essentially over,** and **rate hikes from here will be more cognizant of the new economic environment we're in** with respect to the much higher cost of capital and economic clouds that are circling. Market participants are arguing (kingworldnews for example), **this is the FED's way of telling us, that a slowdown in the pace of future hikes is upon us! In fact, the 2yr yield fell from 4.55% to 4.46% right after while the 10yr yield was off 3 bps. USD did not spike and Gold was stable.** However on the 3rd November yields start to slowly rise again, but the move is contained.
- It is curious that, on the 2nd of November, the bond and equity market didn't get the same message. For equity, it was the worst last 90 minutes of a FED day since 1994 (according statistic of JPM), but bonds reacted differently. **The US bond market have just reached a new negative record: 17% decline over the last 27 months is now the longest and largest drawdown in history.** Somehow we would expect a bottom in the fixed income and ultimately a reverse.
- Mr. Zhao of Alpine Macro argues that **Mr. Powell did not say anything about, if the FED considering the lagged impact of monetary policy, what would be the speed and magnitude for further rate hikes?**
- Mr. Yardeni also states that Powell turned even more hawkish, but he is still convinced that **equity markets bottomed on the 12th of October 2022 and going forward he expects Fed officials soon speaking publicly in less hawkish terms,** effectively toning down Powell's hawkishness. In addition, he expects a possible **red wave in the midterm congressional elections** (Republicans would win), **which would boost the stock market.** Finally, **future inflation indicators should show more signs of moderating, which likewise should support the market.**

FED on the 2nd November 2022 - equity markets should bottom

- Mr. Fugnoli argues in his last blog, that at the end of the day, the FED told us, **they are going to slowdown, but stick on the final target and therefore it is a dovish tone!** He adds, is a clever way to slowdown but do not lose the face. Mister Fugnoli also believes, that equity markets bottomed, though he prefers to bet on the old economy, rather than technology. KTS is fully invested in the SPX Index (our fund based on volatility booster are invested in S&P 500 Futures), value stocks (which are old economy and energy) and the energy space and therefore we like to trade the IT sector via QQQ US, after such correction.
- After reading rumors and analyzing the behavior of global central banks, KTS musts admit, that we are clearly disappointed, since we were expecting a more dovish tone. But, on the other hand, it was a way for the FED to say, they will adapt the pace of rate hikes to economic data and therefore, it is in fact a slowdown for the moment.

Conclusion:

- **KTS was recently analyzing, that fundamentals are extremely weak and getting weaker. In addition, inflation has peaked and should substantially fall in the next months.**
- **Therefore is that a reason to stay calm? Because basically the scenario the FED is waiting for, is going to play out very soon.**
- **We can not short such depressed equity market, especially when we have the high conviction, that future economic data are pointing out the scenario of a more dovish FED.**
- The bond market is telling us this story, the equity market not yet. But we also believe, the **12th of October was the bottom and even equity markets need to consolidate more at this levels, we are convinced in a end year's rally.**

Central banks worldwide - very supportive

- Leaders of South Korea's top financial groups agreed with the country's financial regulator to ensure sufficient liquidity is supplied to the local money and bond markets. A combined USD 67 bn (BRW 95 trn) of liquidity through various programs this year.
- Meanwhile some Euro zone countries (France, Spain and Finland did, but Germany and Austria not) have eased rules for banks to manage the trading of their government debt to help them cope with the challenging markets.

Macro data US - data are weakening, but job data strong

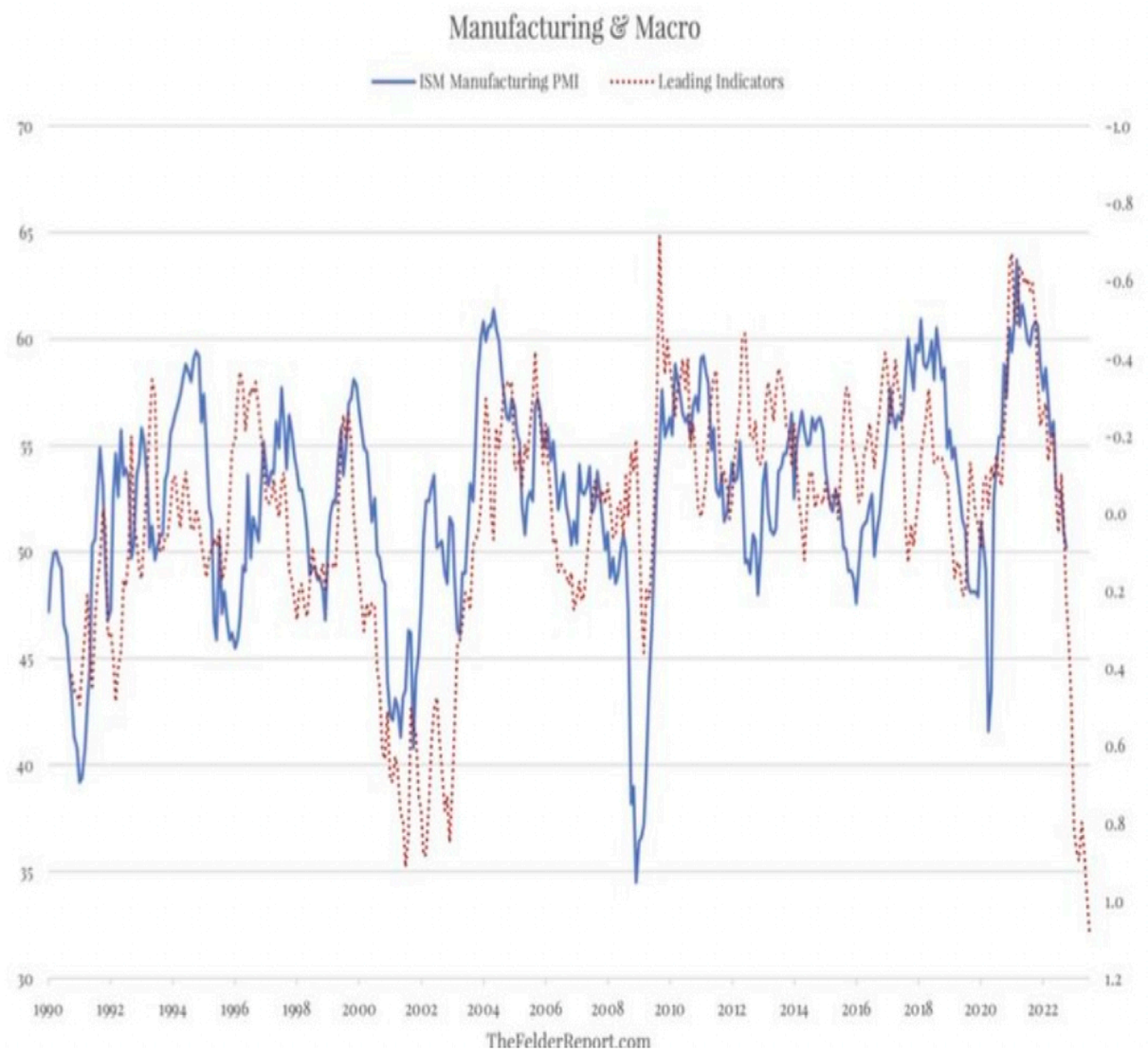
- The ISM manufacturing index fell to 50.2 (expected was 50) and therefore its **lowest level since May 2020.**
- The ISM manufacturing prices paid fell to 46.6 (expectations were 53!) and therefore is the **7th consecutive slowdown and the weakest since May 2020.**
- Also **New orders were down and supplier deliveries plunged to 46.8 from 52.4 indicating excess capacity.**
- Meanwhile the JOLTs Job opening report came a bit above expectations, to 10.7 mio open jobs, showing a solid job market and therefore putting the FED in an uncomfortable situation, facing the risk of wage inflation pressure.
- We are reading, that **Amazon pauses hiring for corporate workforce** and the company had already halted new hires for corporate retail jobs. Amazon has moved quickly to cut costs by ending some projects and shedding warehouse space and is not the only companies. Therefore we are going to see much **more depressed Job opening number going forward** and this should ease pressures on the FED.
- We are reading a good article in kingworldnews.com , referring to CNBC's Leslie Picker report of a research of Kroll Bond Rating agency on private credit, stressing out, that at **a FED funds rate of 5.25%, 60% of companies would see an increase in interest expense (thus 40% likely are hedged) and 16% of companies wouldn't generate enough needed cash flow to service its debt and that doesn't include a recession.**
- We re-connect to the chart of **"zombie" companies of Deutsche Bank in US, where the percentage increased to 24%.**
- Maersk said on earnings release, that it is clear freight rates have peaked and started normalizing and they are expecting a dramatic slowdown in 2023.

Macro data US - job data and labor wage too strong

- On the 4th November equity market are volatile due to the **stronger non-farm payroll**, which exceeded estimates (261k vs 200k expected), suggesting that the demand for labor is still strong.
- In addition, labor wages increased to 0.4% from 0.3% and therefore labor inflation is not coming down.
- Stock markets initially reacted positive and most probably are closing positive, having unemployment rate going up, due to a lower participation rate.
- On the 4th of November equity market are also strong, due to intensifying rumors, that China could potentially ease its Covid restrictions. See more on the subject in the following slides.

Leading indicators pointing out much weaker ISM manufacturing PMI

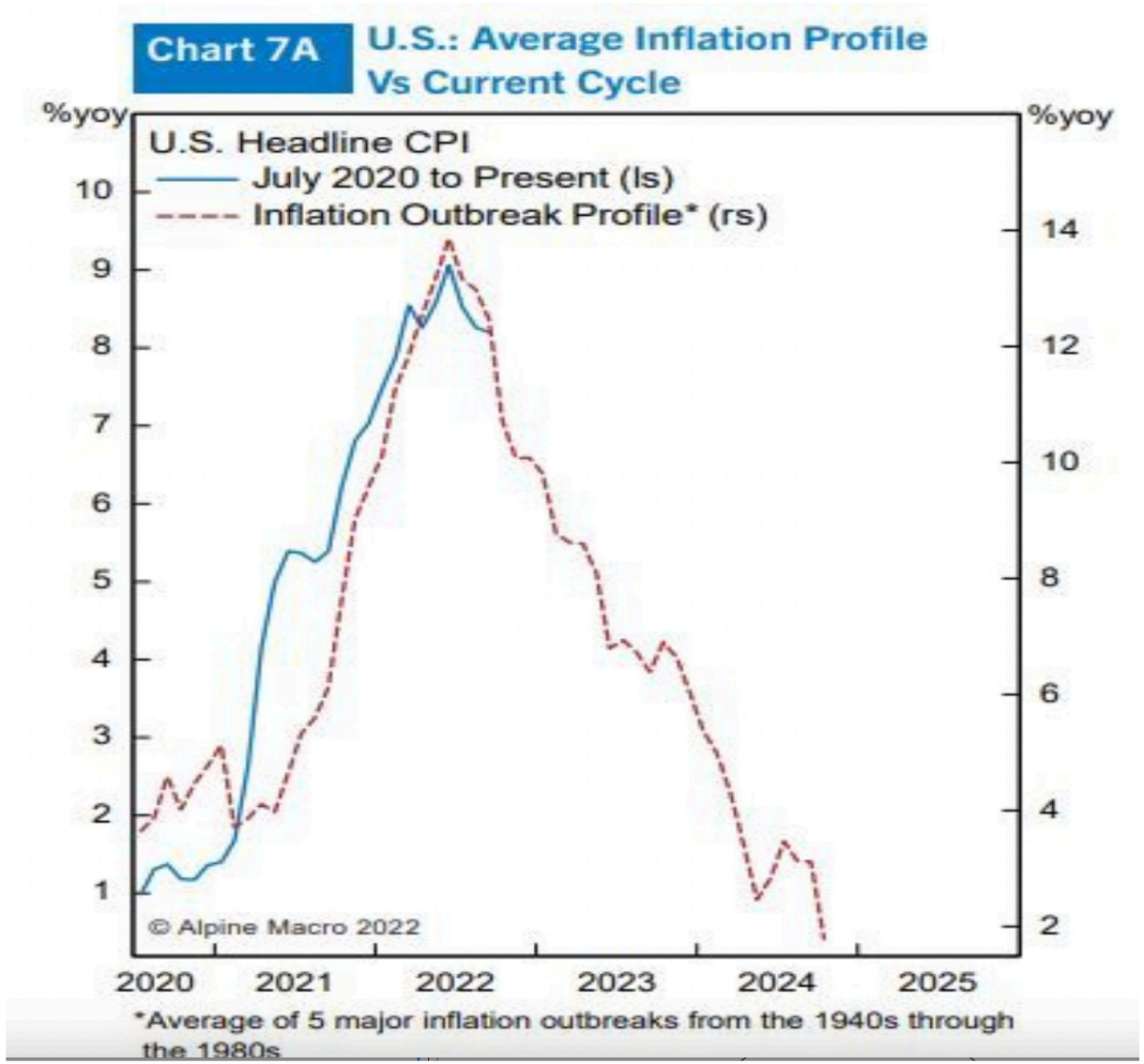
- **The right-hand chart, courtesy Mr. Parvulesco of Quantex, is pointing out a much weaker ISM manufacturing PMI going forward.**



Source: Quantex

Inflation peaked

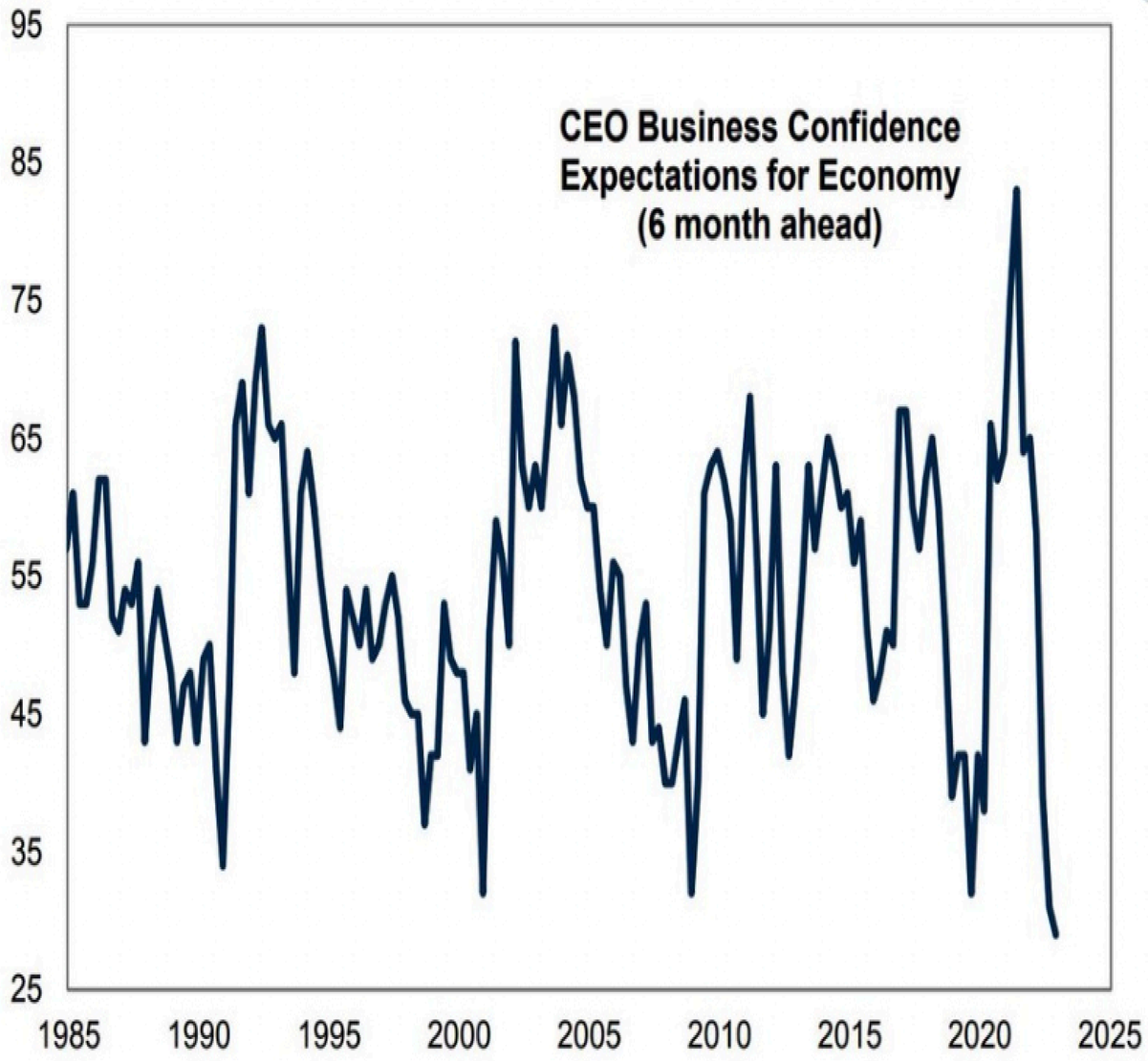
- As we have seen previously, the FED pivot point is going to be only with a lower inflation.
- Mr. Zhao of Alpine macro re-propose their chart on the **average of 5 major inflation outbreaks from the 1940s through the 1980s.**
- The message is, in an inflation cycle, **when inflation peaks out, it tends to fall rapidly and this is what is happening right now.** Fundamental data are pointing out a much weaker economy, which is leading to lower inflation rates.
- Mr. Zhao even asserts: “should we treat Fed Jay Powell as a contrarian indicator, betting against what he says?”.



Source: Macro Alpine

Fundamental data - extreme depressed CEO business confidence

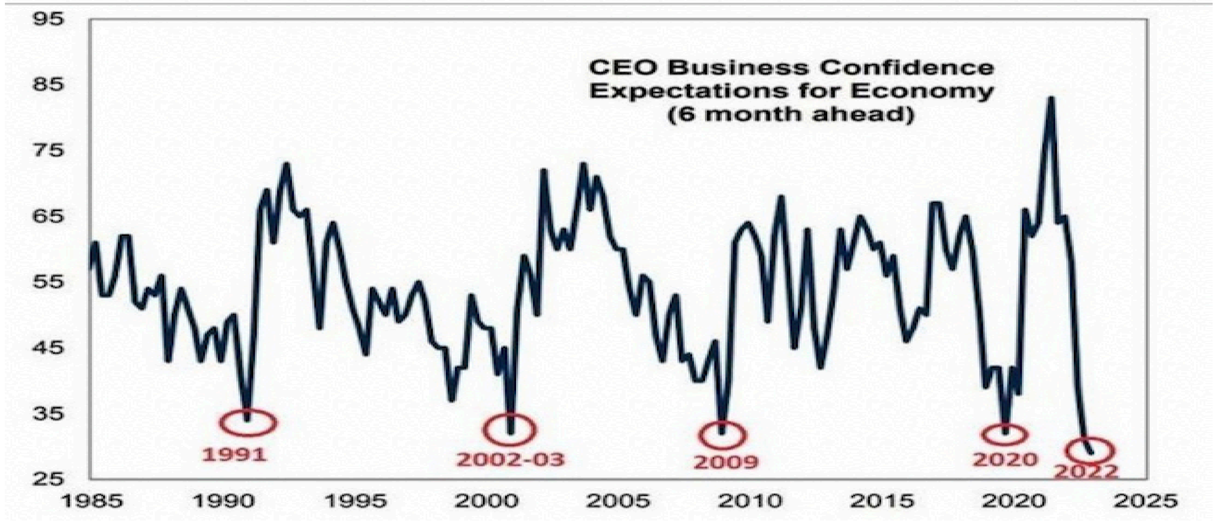
- On the top 10 macro/financial charts of Mr. Barraud, we have several charts on the **weakness of the U.S. Housing market** (we had similar one in our last weekly report) with residential investment down 26.4% in Q3, NMHC market tightness index collapsing in October (almost at levels than GFC 2008 and recession in 2001-2002), land prices falling 9% in the last 3 months, mortgage purchase applications index fell to the weakest reading since early 2015.
- But we would like to mention again the **CEO business confidence expectations for economy (6 month ahead), which is lower than during GFC, pandemic and technology bubble.** The CEO confidence index has never been so depressed.
- On one hand, as contrarian, we have seen the worse and it should only be better, especially with central banks at a pivot point, on the other hand, we can not expect a strong economy for the next 6-9 months. **Equity markets are normally discounting 6 to 9 months in advance?**



Source: Goldman Sachs / Mr. Michael A. Arouet

Fundamental data - extreme depressed CEO business confidence

- Goldman Sachs compared the lows of CEO business confidence with the development of the S&P 500 Index and as we can notice in the comparison below, **extreme low levels of CEO business confidence coincide with the bottom of equity markets.**

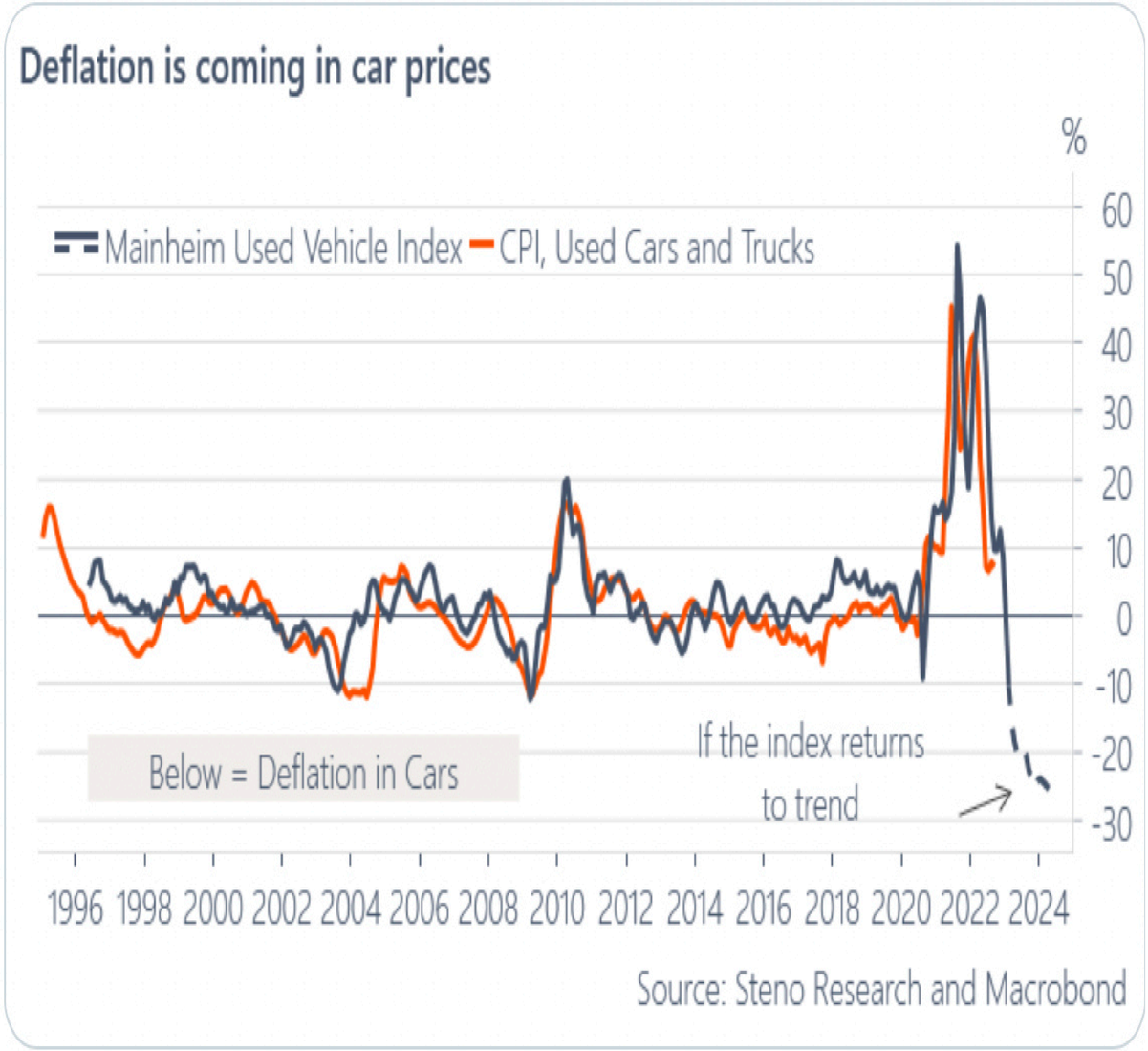


Extreme low levels coincide with

Bottom of equity markets. (Source GS via Mr. Tanase)

Deflation is coming in car prices

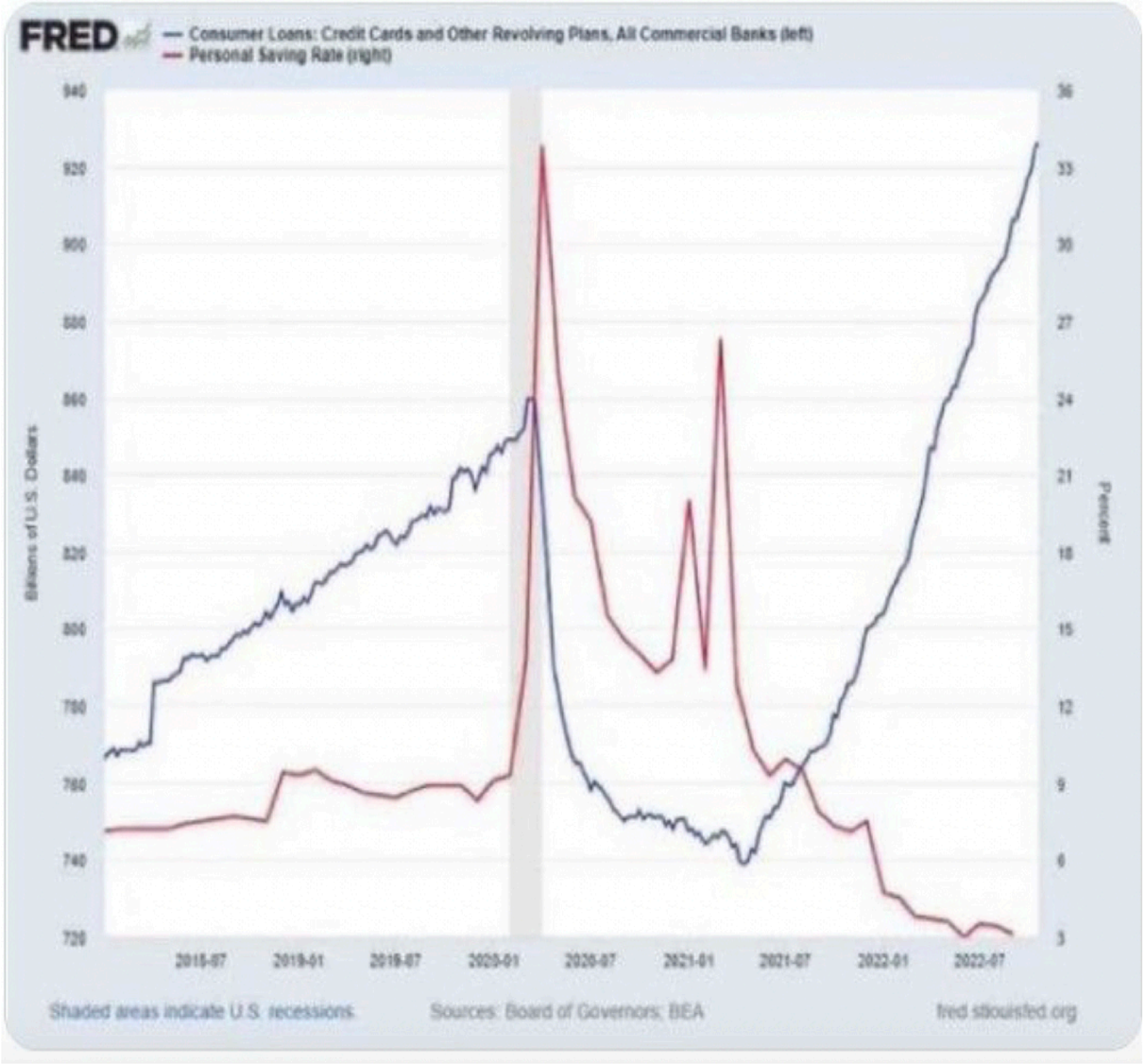
- On the right-hand chart, courtesy Mr. Larsen/Macrobond, used cars and trucks prices, which were the first inflation's problem, having massive purchases at the beginning of the normalization process coming out from lockdowns, **is now going into deflation.**
- Many experts were warning of such trend and the main issue are now the open loans on cars, which were done by 140% the price at the very beginning. **This could cause financial losses to US banks.**
- **But the positive side is, US CPI is going to fall.**
- In addition, as we can see in the next slides, **if China would completely reopen the economy and finally leave Covid zero policy,** we should finally have no supply disruptions and further deflation on the short term.
- **On the longer term, commodities and oil prices would rise, a reason more for KTS to stay invested in the sectors.**
- Also kingworldnews.com report similar statistics.



Source. Macrobond / Mr. Larsen

Credit card debt vs savings rate in USA

- The right-hand chart shows the alarming situation of US consumers.
- **Due to the high inflation, US consumers are using the maximum limit of credit cards, but savings are gone.** US households are increasingly leaning on credit cards to afford basic necessities since incomes have not kept pace with inflation, says the CIO of Lombard.
- The situation is extremely stretched and the future outcome is not promising. This is a risk, which we have to take into account in our fundamental analysis.
- Mr. Monier, CIO of Lombard Odier even asserts, US customers are running out of cash.
- **US spending was still strong, but analyzing this chart, we agree, it is near exhaustion. Lombard Odier foresee a recession in 2023.**
- **US consumption is 68.2% of the US GDP.**



Source: FRED/Syz Group/Lombard Odier (CIO Stéphane Monier)

Macro Europe, German industry leaving the country

- A good article in the newspaper Focus online explains, how the **German industry is leaving the country for places with better energy and labor costs.** BASF for example keeps production investments in China, despite political tensions. Those are very negative news for the future of Germany, which is also increasing indebtedness in order to help lower incomers on high energy costs, but with future lower tax income and with plans to increase taxes for top wealthy citizens, which can leave the country in no time (the top 10% is responsible for 2/3 of German tax income), it will be difficult to improve the financial situation of the German government, which is risking to start a vicious cycle, like it started already long time ago in other European countries such as Italy, France and Spain.
- The newspaper Handelsblatt writes that US investors and entrepreneurs are blaming Germany, to not being an attractive location for business anymore. Energy supply is unstable and expensive, not enough workforce, old infrastructure are the main reasons.
- As we have seen last week, European natural gas prices are currently even negative, but our expert was arguing, it is too early to celebrate, because forward prices are still very high.
- **Mr. Robin Brooks explains, that the current extreme negative natural gas prices are not due to abundance of gas, but rather due to lack of storage.**
- Meanwhile we are reading the headline in WallStreet Silver (The Observer), that more than 2 million UK households are in debt due to their electricity bills and the winter hasn't even started yet.
- The **Eurozone October CPI accelerated to 10.7% from 9.9% in September and energy prices continued being the main driver,** but food and imported industrial goods all pushed prices sharply higher. We believe that the weak EUR is the main cause.

Macro Europe, Mr. Putin would be ready for a dialogue

- German industry cut its gas consumption by 19% in September (source Hertie School's Centre for Sustainability). A further reduction in as consumption is likely in view of persistently high gas prices. Apparently, industry operators charged more for their output, switched to alternative fuels or substituted energy intensive products with imports.
- The fact that industries are substituting energy intensive products with imports, re-connects to the first points, where many German industries are leaving the country.
- The **private households in Germany increased gas savings to 36% y/y in September!**
- Last week we mentioned Russia claiming, Moscow has never said anything proactively about the possible use of nuclear weapons. This week we are reading an article on the German newspaper amp-ntv.de, that Mr. Putin would like a dialogue with Mr. Biden and Kiev, but Mr. Biden apparently refuse to meet with Mr. Putin. Sounds like Russia is really ready for a dialogue.

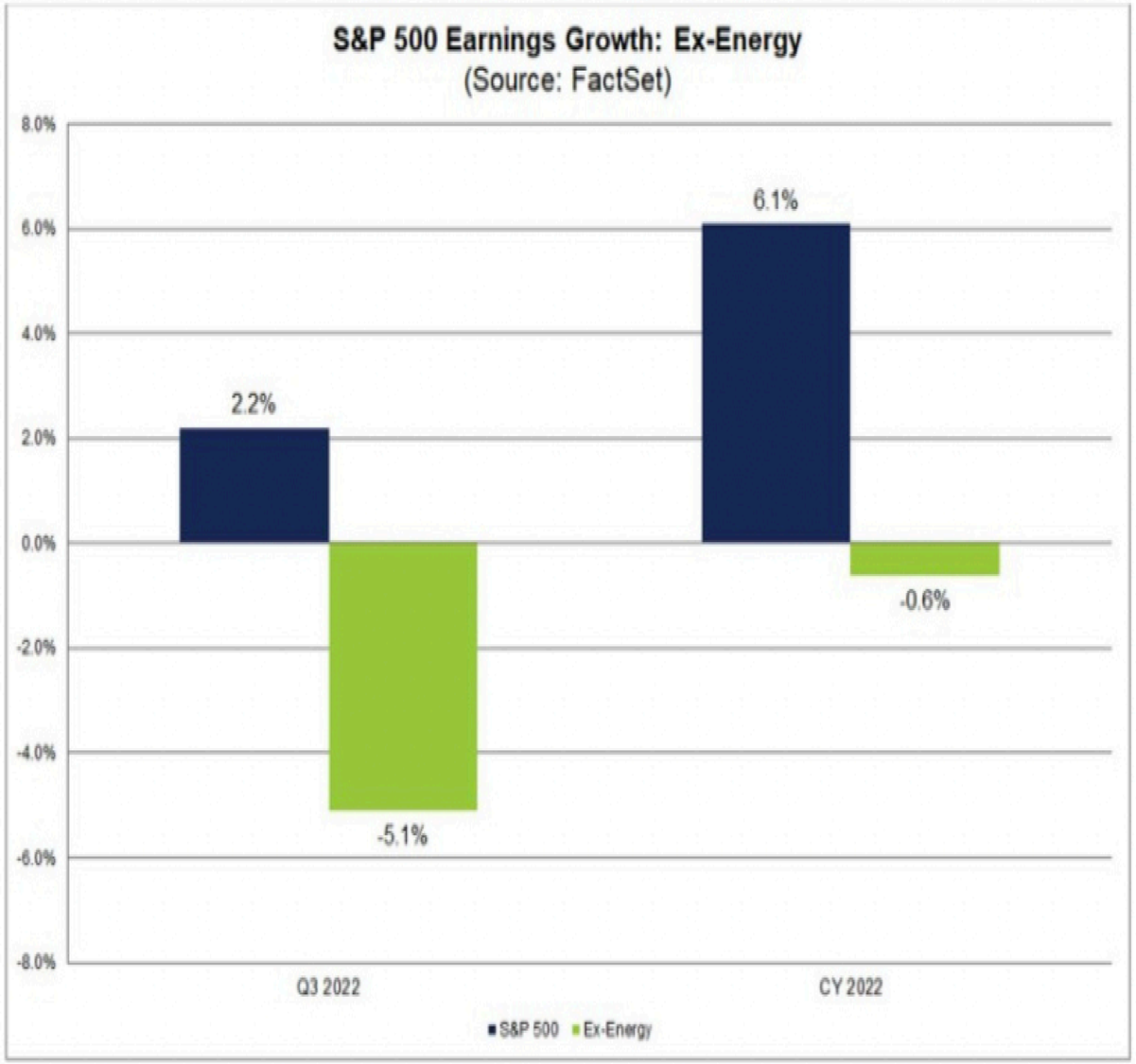
How Russia pays for its war

- The New York Times shows a chart with **Russian exports after the war began and we can all notice, that the value of Russian exports has actually grown,** in particular to Turkey, India, Brazil and of course China. **The Netherlands and Italy are the third biggest buyer of Russian oil, after China and India:**
- It is true, by volume, **Russia's imports** plunged as sanctions and trade limits went into effect, but a few countries have deepened their relationships with Russia since the invasion: **Turkey have increased by 113% (and we all have seen, indirectly also Italy, exporting to Turkey) and China by 24%.**
- The green German foreign minister Ms. Baerbock is still convinced to kneel Russia, but numbers are showing something different. On the contrary, if we analyze inflation numbers in Europe, we have a tremendous dilemma, worse than USA. Perhaps is it finally time for Europe to evaluate the possibility of a diplomatic solution?

China and India are the biggest buyer of Russian oil (EEAGLI/NYT)

71% EPS beat rate

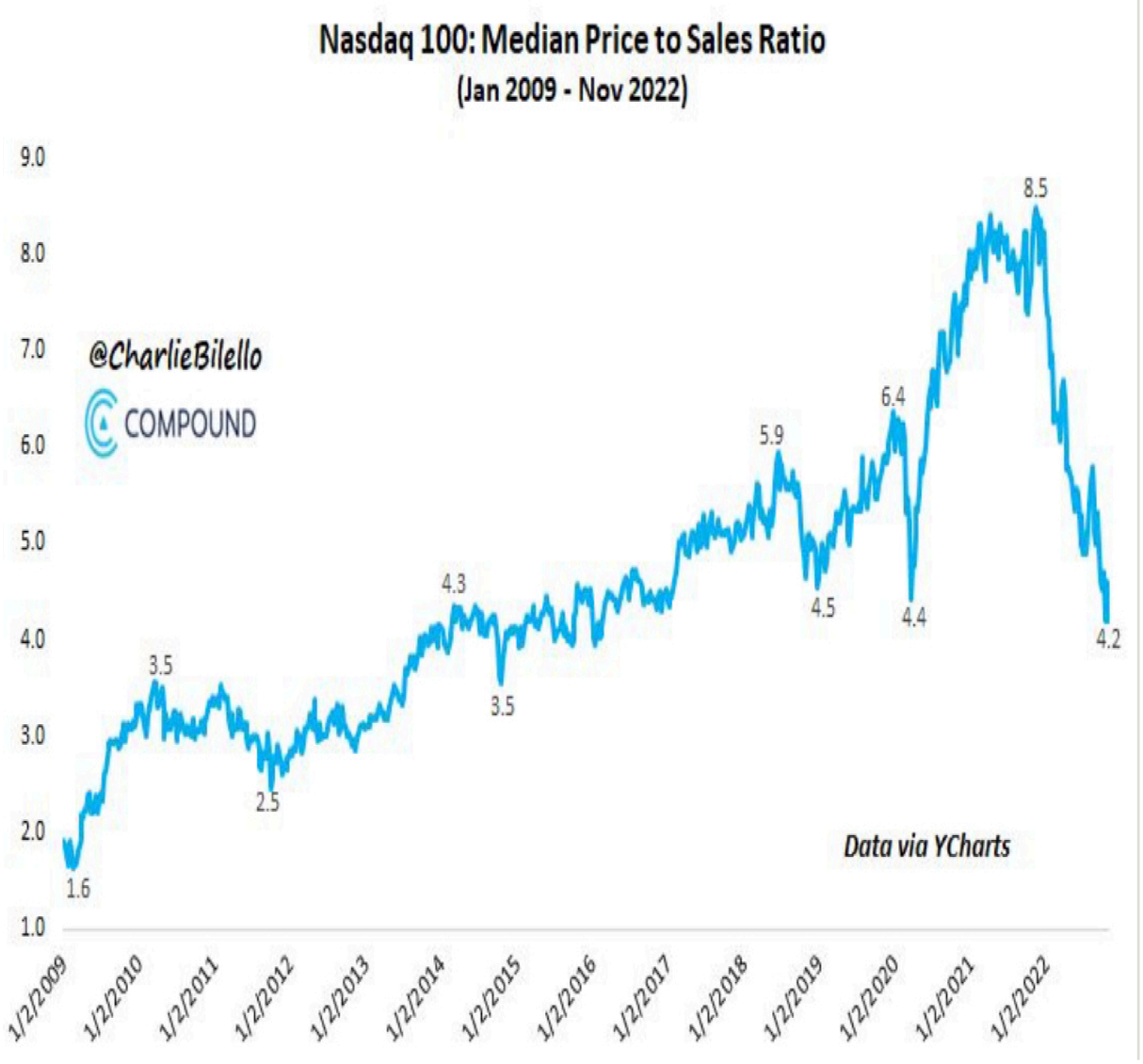
- Currently, over the half of S&P 500 Index companies have reported Q3 results and according to the statistic of Mr. Zacardelli, 71% beat on EPS, 68% on revenues.
- **Ex Energy, SPX reporting a -5.1% EPS growth rate (Bloomberg chart show S&P 500 ex-energy forward earnings are back to their January level at 228 USD from highs 240 in June 2022).**
- Most of outlooks were weak, but equity markets already discounted it. **Of course a deep recession is not discounted yet, but we will see in the next slides, it is only 1/3 of the total return of equity.**
- The FED is keeping the “hard line” and therefore now there is a serious risk of a deep recession, which is still not discounted. Other central banks slowdown the pace, but the FED is still too ambiguous on the real moves she is going to take. As argued, perhaps is the start of smaller steps adapted to the development of the economy.



Source: Mike Zacardelli via Syz Group

Median price to sales ratio of the Nasdaq 100

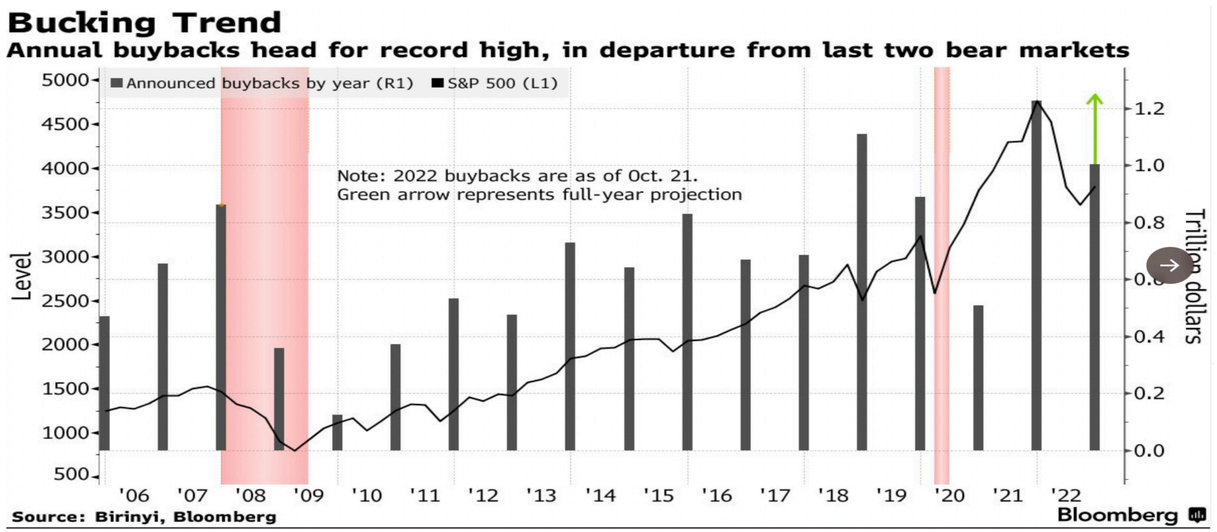
- The median price to sales ratio of the Nasdaq 100 has moved down to **4.2x, which is its lowest level since February 2016.**
- It peaked last November at 8.5x and the Nasdaq 100 Index is down over 35% since.
- With giant tech companies having a lot of cash and buying own shares, we can assert, that the IT sector is slowly but surely attractive.



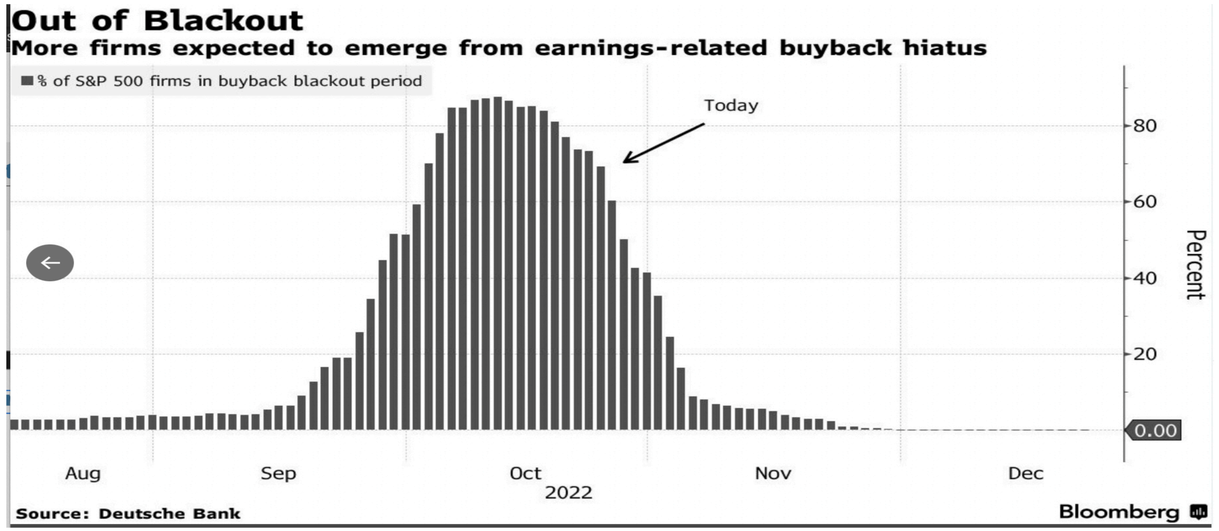
Source: CharlieBilello

The power of share buy back programs

- As explained last week, 48h after results, companies can start to buy back their own shares.
- As we have seen, many FAANGS experienced correction up to 20% or more and are starting becoming value stocks, but with high levels of cash (net cash) in the balance sheet and, except Meta, most of them still have a solid business.
- Therefore, companies stopped some projects and are going to use the liquidity to buyback their own shares.
- According to Mr. Lance Roberts' tweet, **25% of the S&P 500 Index come out of blackout window and there are roughly USD 5 billion a day coming on the buy side** through year-end and the total for the year 2022 going to be over USD 1 trillion in buybacks.
- It is probably not a coincidence, that now **S&P 500 up sessions are getting more powerful than down days** (chart Bloomberg not included). On one side, sellers have become exhausted, but on the other side, **investors could underestimate the "power of share buyback programs"** .



2022: will be the next record high in share buyback program

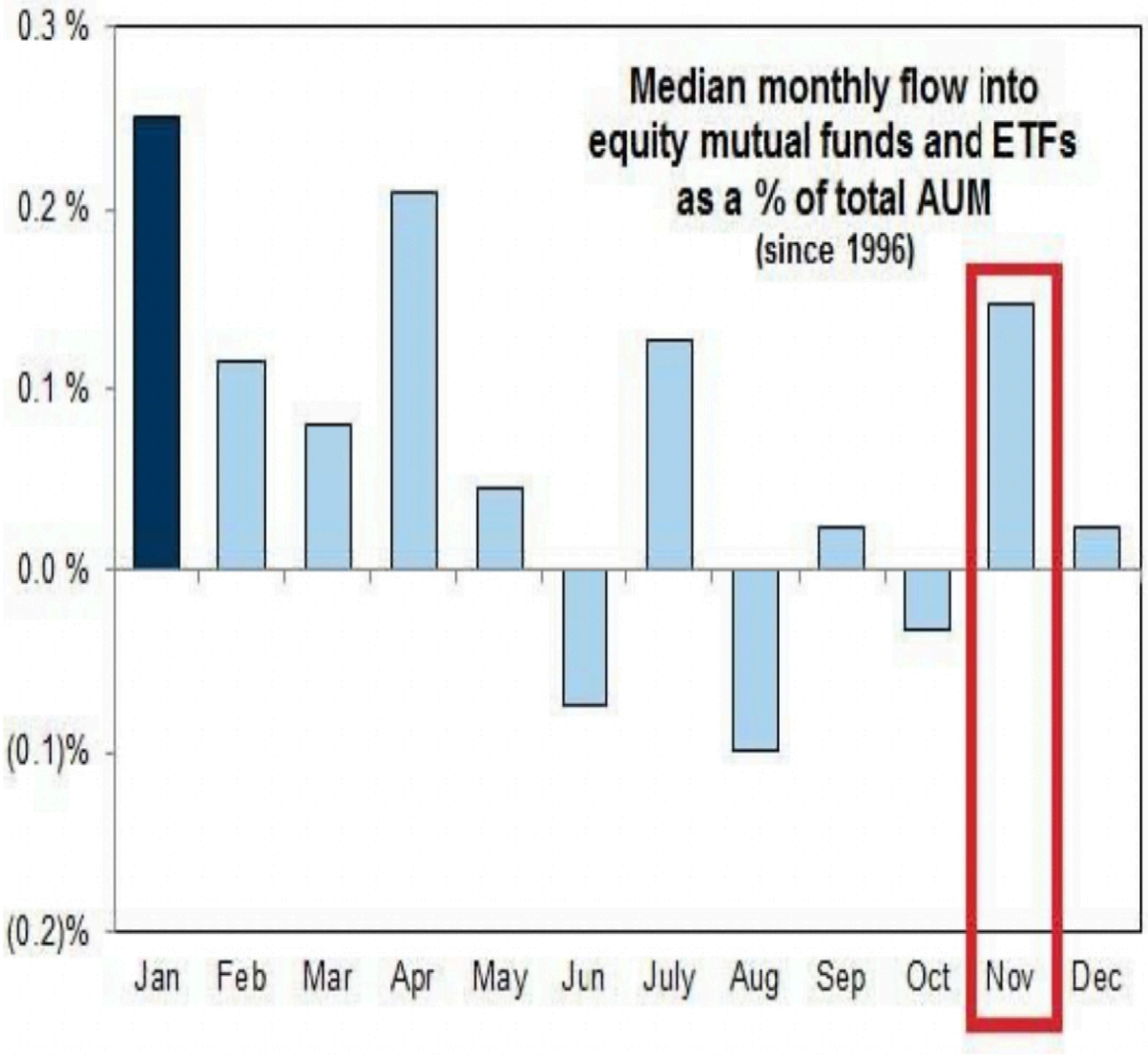


After the result season, companies can buy back again own shares

Up to USD 20 billion of daily stock demand until year-end

- According to Goldman Sachs, mr. Scott Rubner, there is **USD 20 bn of daily stock demand until year-end.**
- The arguments are: largest sellers have completed and + USD 20 bn worth of daily equity demand is kicking in:
  - **USD 12bn from systematic**
  - **USD 5bn from shs buyback programs**
  - **USD 3 bn from retails**

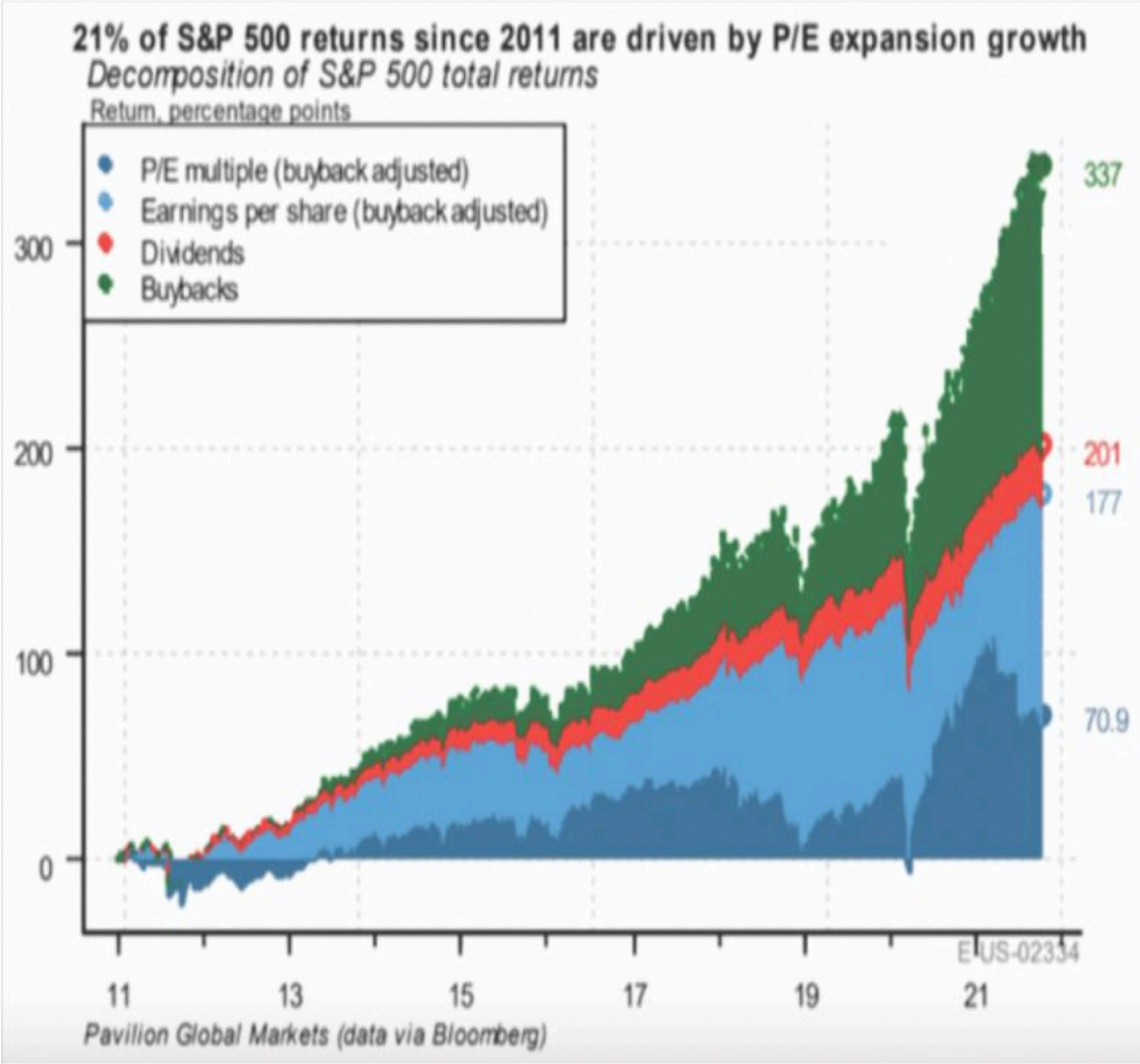
- Over the last 30 years, +20 bps of new money comes to the market every November, on USD 22 Trillion in assets, this is USD 44 billion or new USD 2.5 bn per day.
- Those number are not taking into account any gamma squeeze in case shorties need to close positions. Although after the FED speech of the 2nd of November, most probably professional investors will not be under pressure to increase equity positions, not yet.



Source: GS via Syz Group

Share buyback programs are responsible for 40% of total returns

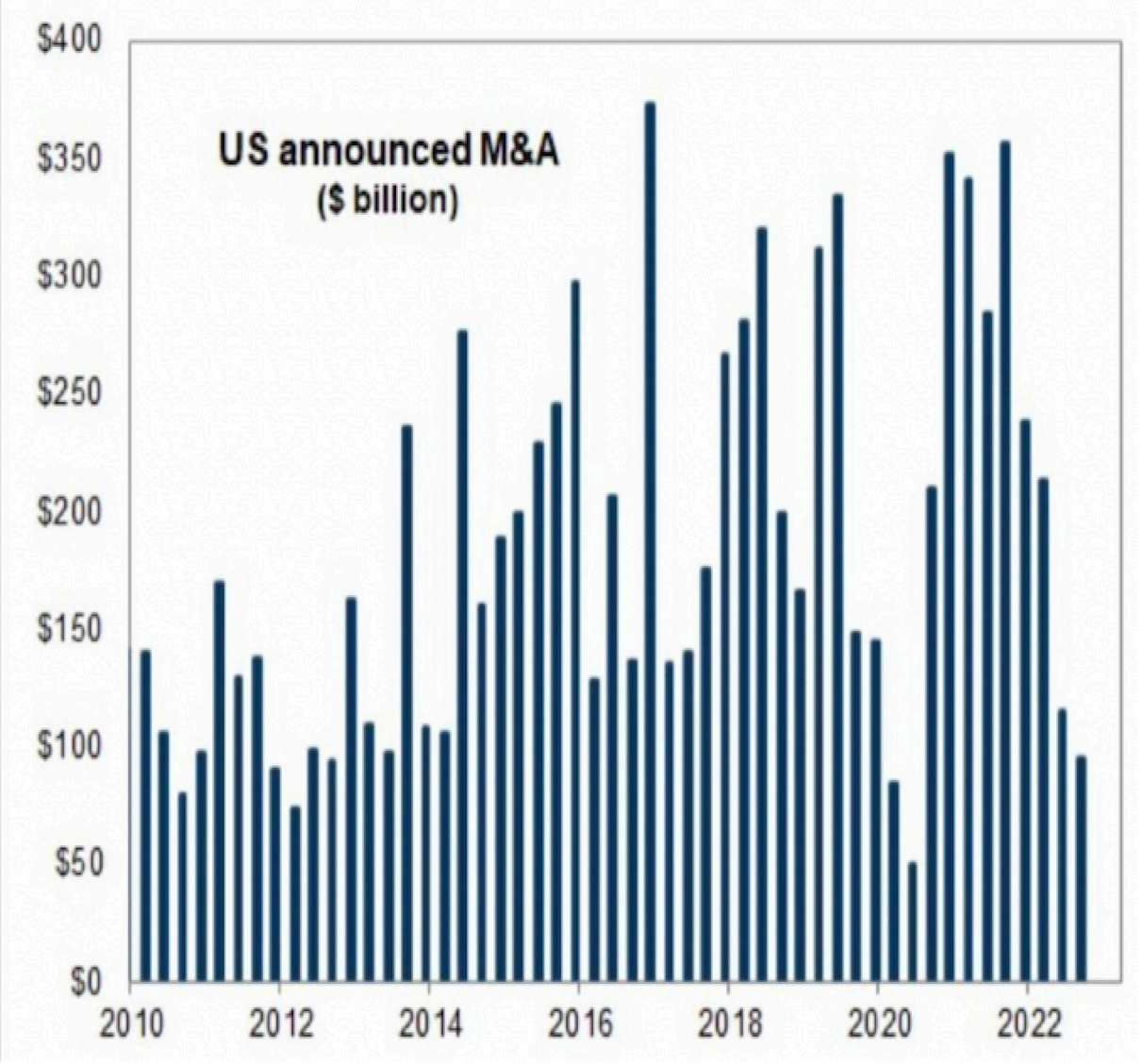
- Mr. Rowles posted the chart of the distribution of S&P500 index performance during the last 11 years (KTS already posted multiple times this year).
- **P/E multiple expansion account for 21.03% of returns.** If we take into account, that inflation is going to fall and therefore also yields, **multiple expansion could help triggering an equity market rally.**
- But the biggest portion is **share buyback programs, which accounts 40.35%** of total returns during the last 11 years. As we have seen in the previous and next slides, **during the next 2 months we will experience substantial inflows from such programs.**
- Therefore market participants are arguing that if **EPS** would fall further, from the already strong disappointments in Q3 and latest outlooks, mostly by FAANGS, **it would count "only" 1/3 of the total return.**
- Dividends may fluctuate, but are only 7.12% risk on return potential.



Source: Pavillon global Market via Mr. Rowles

Companies are using liquidity for shs buyback rather than M&A

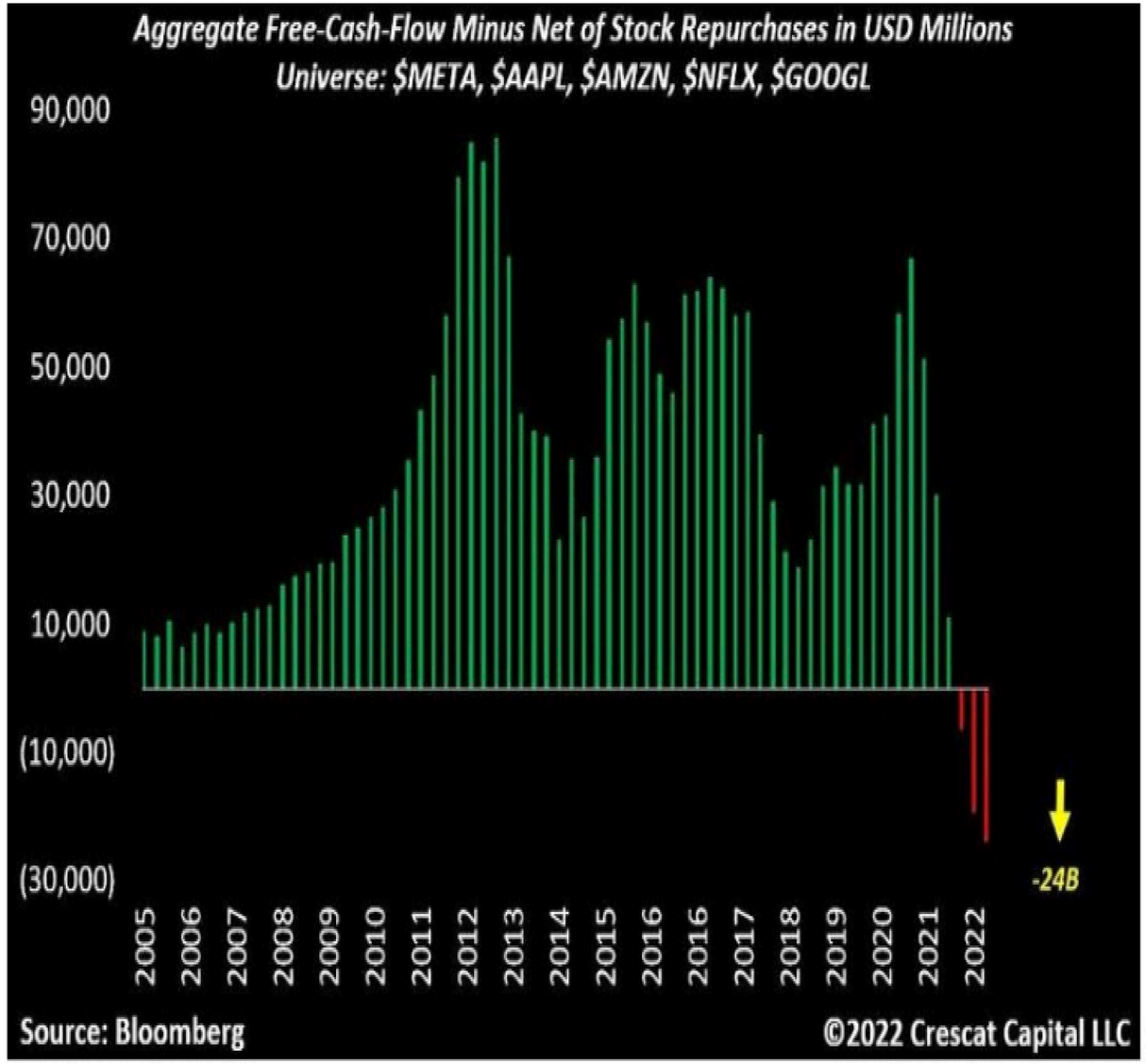
- Mr. Lemand rightly argues, that companies should use liquidity for M&A rather increasing shs buyback programs.
- On the right-hand chart, courtesy Mr. Lemand and GS, we can notice the collapse in M&A activities, but at the **same time buyback authorizations is up 8% year/year** (chart GS buybacks trading desk not included).
- Recently we were showing a chart of **Apple, which has bought back USD 549 billion in stock over the past 10 years. That amount is greater than the market cap of 494 companies in the S&P 500 Index** (source: Charlie Bilello / Via Syz Group not included in this weekly report).
- **In any case, if not via M&A, but via shs buyback programs, this money flow support equity markets.**
- **Meanwhile Canada is going to impose 2% tax on stock buybacks as of 1. January 2024.**



Source: Dealogic, Goldman Sachs via Mr. Ryan Lemand PhD

FAANG stocks buybacks higher than FCF

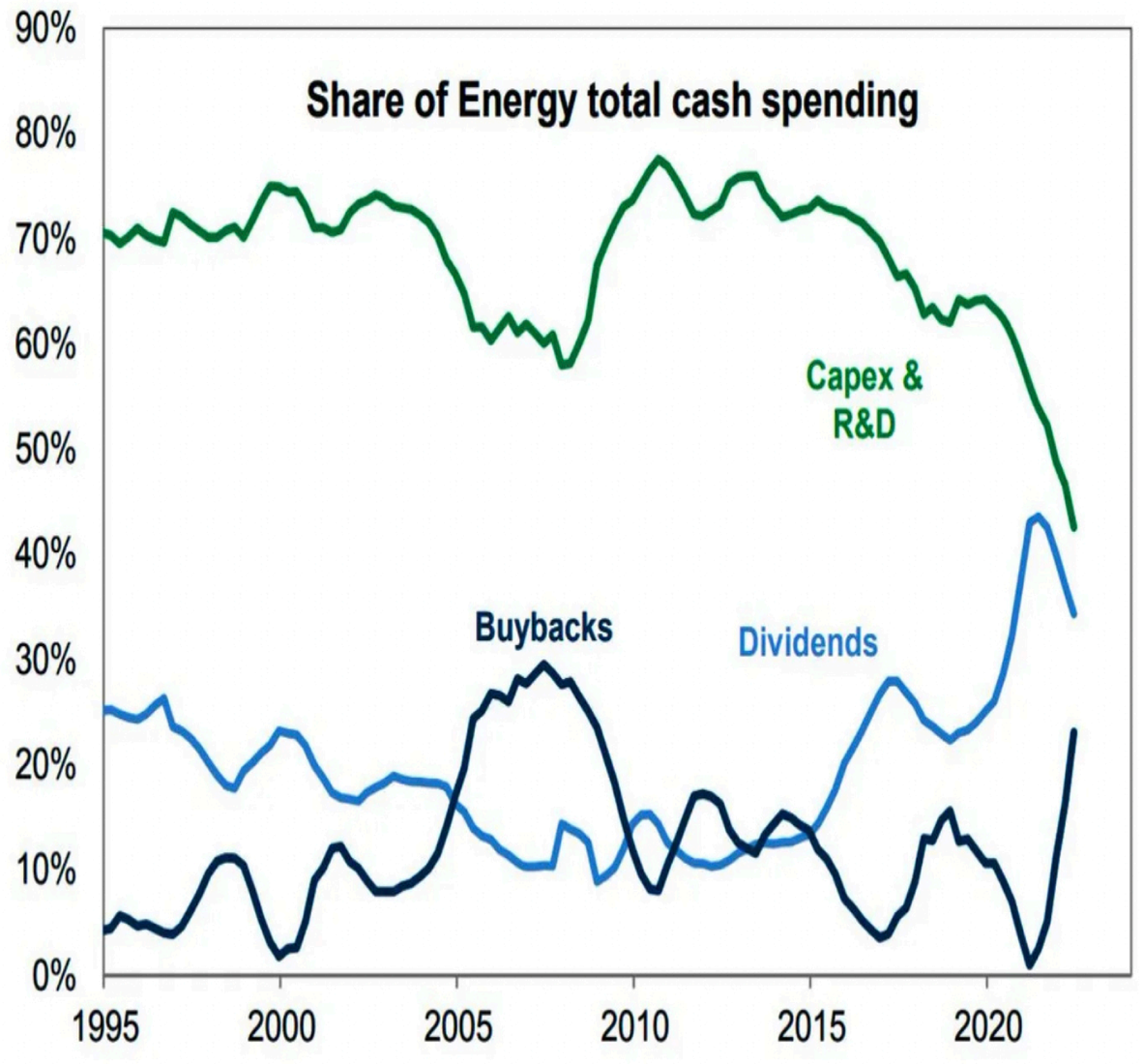
- The real issue on longer term for FAANGS stocks is the fact, that currently according to statistic of Crescat Capital, FAANG **are spending more money in buying back their own shares, than the generated FCF.**
- This is very negative on the longer term. Most of liquidity should be meant for innovation or buying smaller companies with interesting technologies at attractive prices, especially at current valuations.
- On the other hand, Meta is definitely investing cash into innovation, but market participants are not patient and fear the future outcome. We understand that the metaverse is a tremendous bet and capex are huge, therefore, if it would not workout, or take much longer than expected, it is going to hurt financially the company.
- In addition, Faangs are experiencing the slowest revenues growth yoy.



Source: Crescat Capital

Energy companies increasingly focused on share buybacks

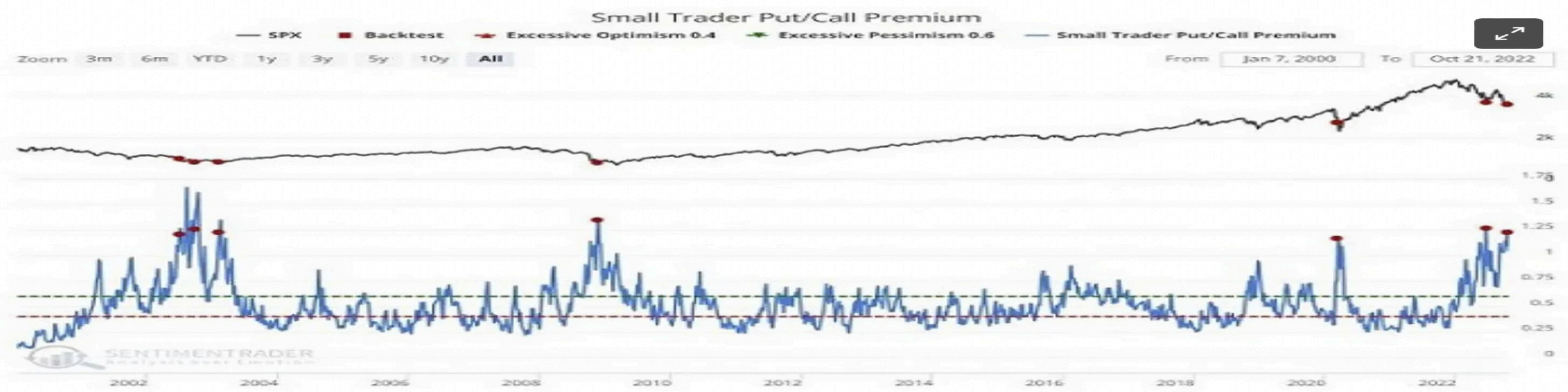
- Energy companies had to reduce capex due to lower oil prices during the pandemic.
- In addition, nowadays it is difficult to increase capex with new regulations on carbon-zero emission.
- **Therefore, energy companies are increasing share buybacks and not investing in R&D or capex.**
- This is not good news for consumers, because we need a lower oil price and therefore new oil production/supply, which can not be increased, if capex is not increased.
- Meanwhile this is positive for KTS's exposure in the sector.
- In fact, the **energy sector is over 50% YTD, vs equity market down over 20%**. Our green active basket is flat, vs green investment vehicles on average down also over -20%.
- Meanwhile **Biden's administration is threatening oil&gas producers with a tax on their "excess profits"** if they do not boost US production and refining capacity. **A windfall tax would be difficult to push through Congress.**



Source: GS vis Mr. Thomas Callum

Small trader put vs call premium

- Below we attach an interesting chart, showing the **premium of put option vs call** (courtesy the weekly S&P 500 Chartstorm of Mr. Callum Thomas).
- The argument is very simple. In **bear markets put options are more valuable than call options**, especially when everyone wants them and especially usually at the worst possible timing. **Notice the performance 1 year later after the signal occur.**

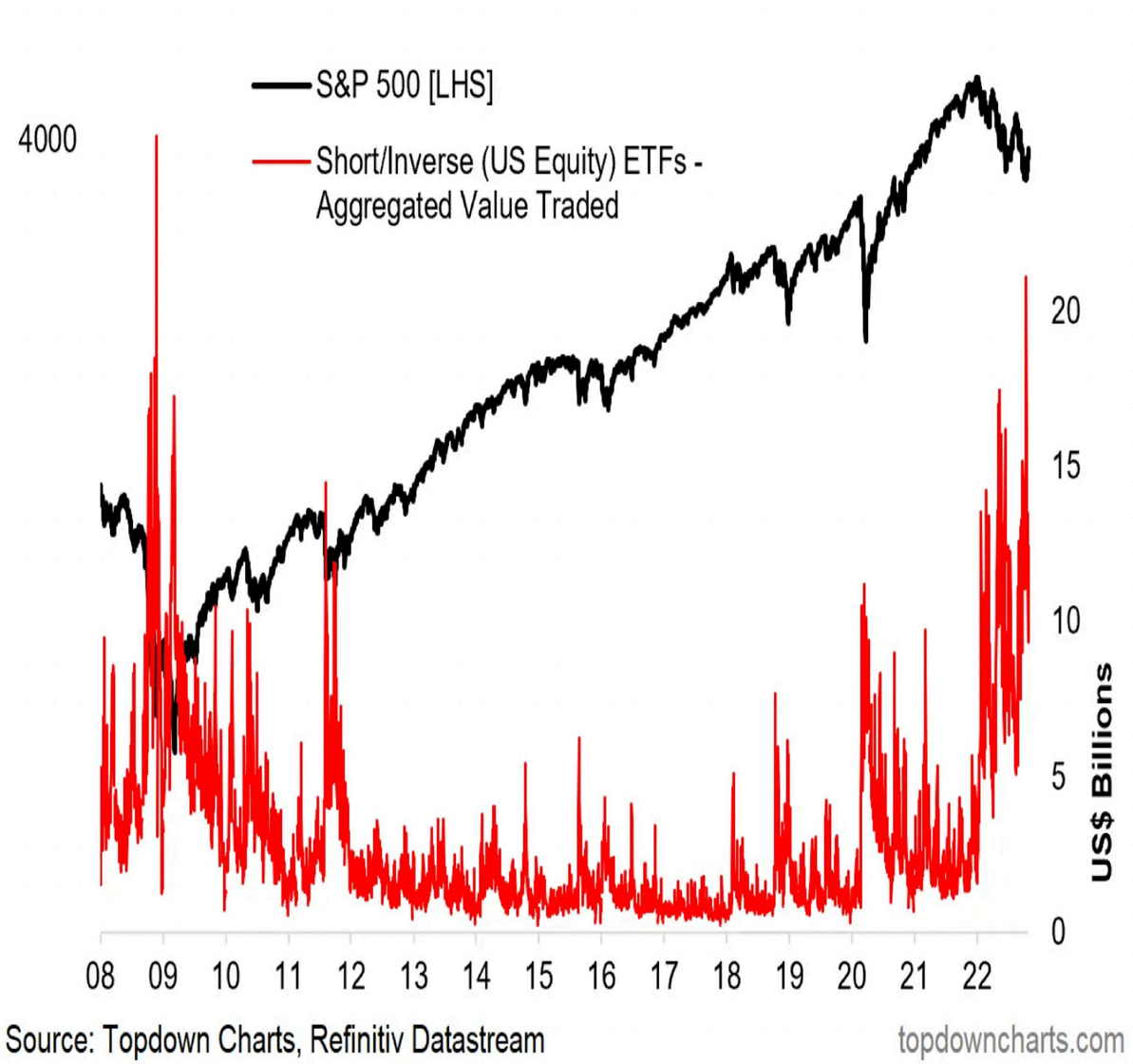


	1 Week Later (%)	2 Weeks Later (%)	1 Month Later (%)	2 Months Later (%)	3 Months Later (%)	6 Months Later (%)	1 Year Later (%)
Average Returns	0.30%	-0.25%	1.31%	6.76%	5.81%	7.96%	27.86%
Median Returns	-0.39%	-0.97%	3.76%	6.94%	8.66%	10.87%	36.34%
Win Rate	43%	50%	67%	83%	83%	60%	100%

Over 27% positive performance 1 year later (source @jaykaeppel)

Volume of leveraged/inverse ETFs at extreme levels

- The **volume into short or inverse ETFs is at highs**, like 2008 and higher than the pandemic, therefore confirming that investor's sentiment is still extreme bearish.
- KTS believes, like for the highest volume ever into put options, market participants also use such **ETFs to hedge long positions, instead of selling due to higher profit taxes in the US since January 2022.**



Source: Topdown Charts / Mr. Callum

Technical analysis

- Market participants are arguing that the Dow is already overbought and CNN fear and greed Index was at greed levels (61 points out of 100) before the 2nd of November, is now also falling again to Neutral (55).
- But the **BofA Bull&Bear indicator, which is indicating the sentiment amongst professional investor, is still at 0 at extreme bearish.**
- We are reading with pleasure, that we **have just experienced the best October month in history (over 100 years)**, according to statistic of Mr. Budelmann (+14.3% for the S&P 500 Index). In addition, **October 2022 was basically also the best month in history**, only January 1976 was better (data since 1930).

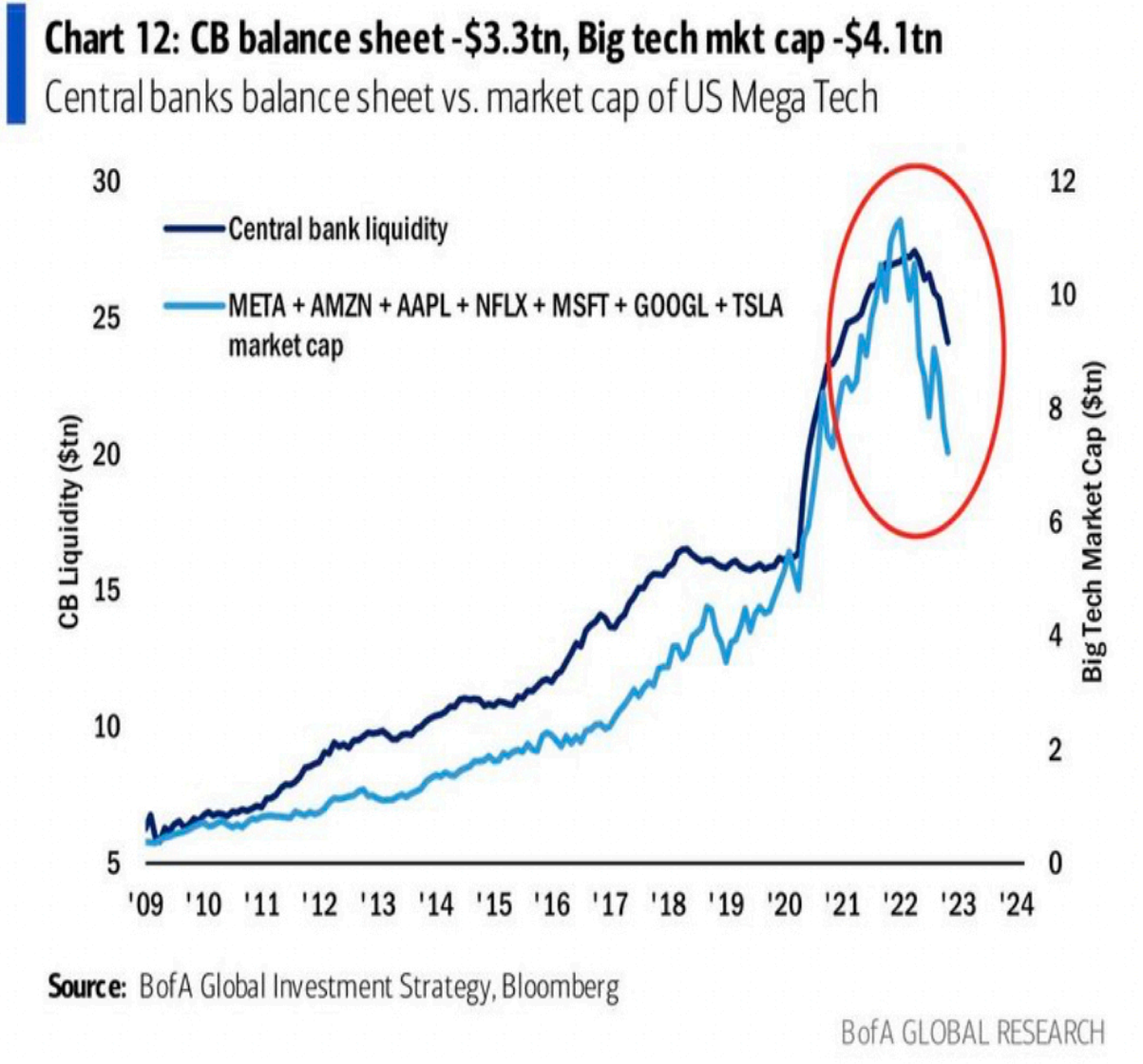
Technical analysis

- KTS still believes, the low of 12th October is a strong support, being the 200w moving average, which was the strongest support for the whole bull market since 2011.
- In addition 3’500 points was the 50% Fibonacci retracement. We believe, the S&P 500 Index should not fall under 3’500 points and the first upside resistance is the 200d moving average, which coincide also with the downtrend line: 4’097 points

The low of 12th October 2022 are a strong support: 50% Fibonacci and the 200w moving average. Only over 4’326 is a major breakout, the start of bull market

Correlation central banks balance sheet vs. Market cap of US mega Tech

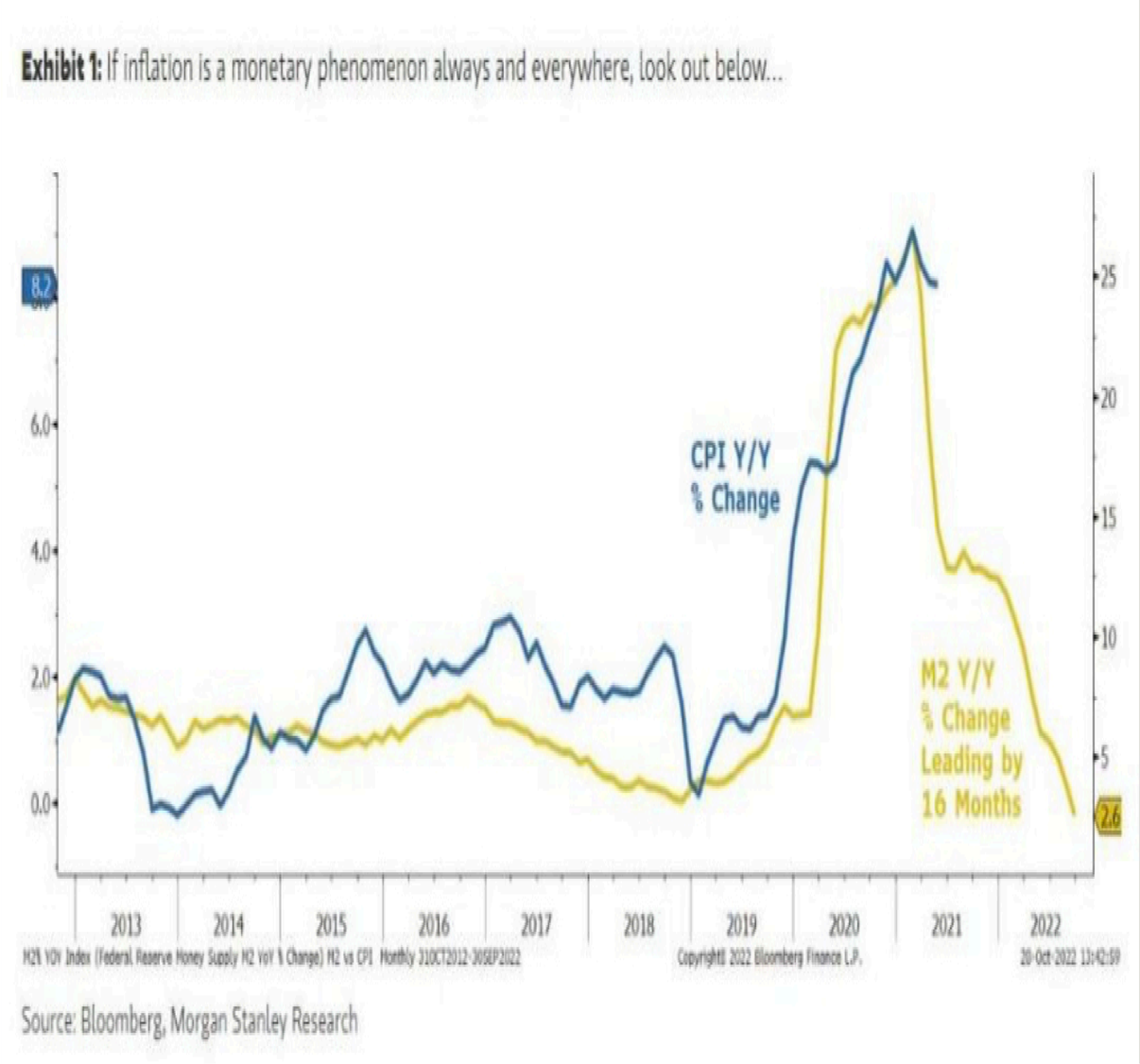
- Market participants always argued that equity markets, especially **very speculative investments like SPACs, Cryptos, etc. will increase only if M2 and central banks balance sheet increase.**
- With QT ongoing, liquidity is falling and therefore also money to be invested.
- The right-hand chart, courtesy BofA via Syz Group, shows the correlation between the central banks balance sheet vs. market cap of US Mega Tech and we can analyze, that **balance sheets is down USD 3.3 trillion vs USD 4.1 trillion in market cap of US mega caps.**
- Now after the correction, **we have major companies buying back shares and supporting**. Most probably, with yields coming down due to future lower inflation, it will be an additional trigger for higher equity markets, **especially the IT sector.**
- **But new highs would be possible only with central banks expanding the balance sheets again.** But some well known investors expect new highs mid 2023.



Source: BofA via Syz Group

Correlation between M2 growth and inflation

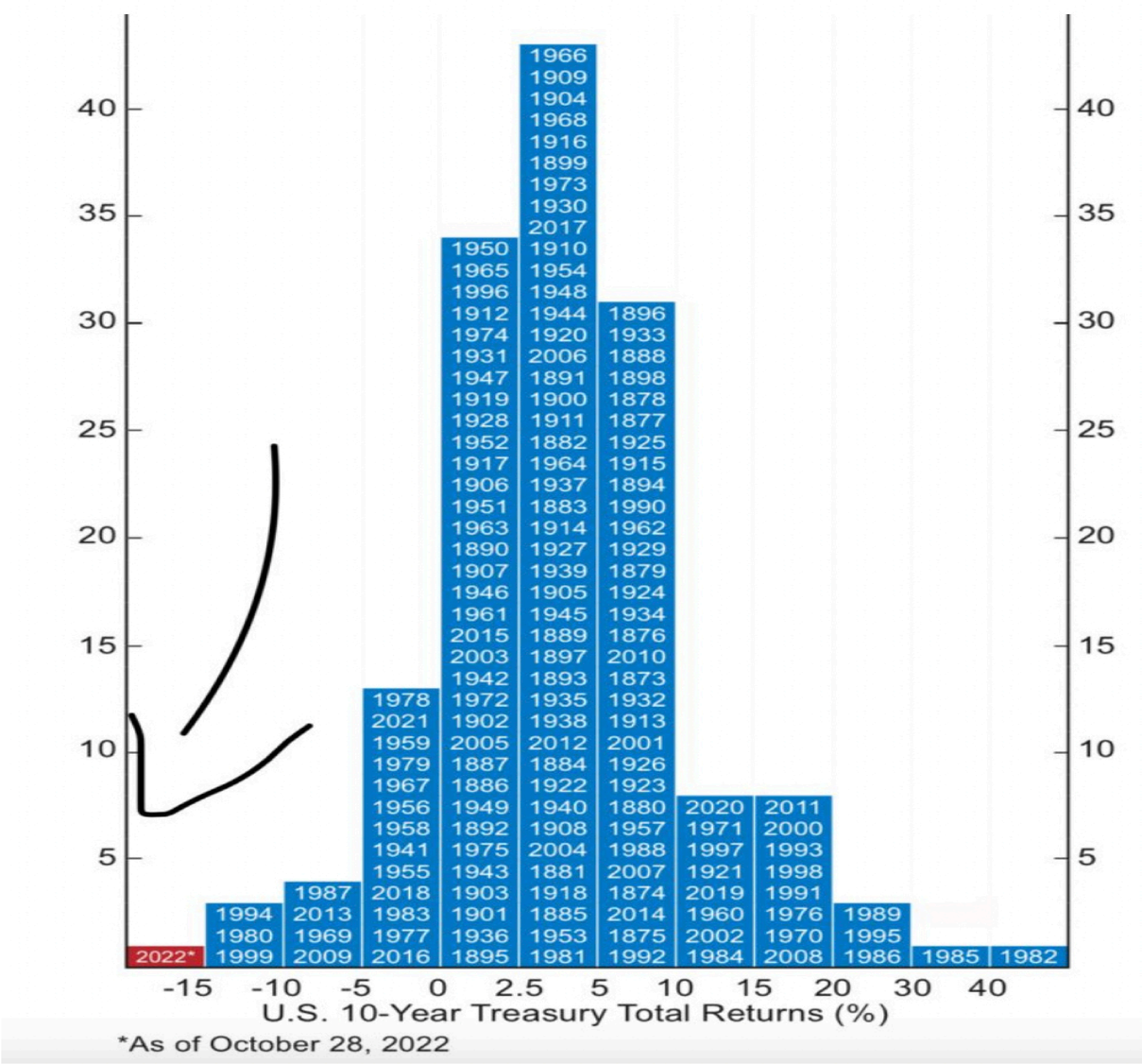
- As we have seen, the significant fall of M2 money supply and central bank balance sheets is negative for equity.
- On the other hand, the **extreme and fast fall of M2 growth is pointing out a extreme fall of inflation,** according to historical correlation.
- Lower inflation means lower yields and therefore should help **equity to rally based on higher valuations** (WACC discount rate on DCF models is lower, leading to higher valuations).
- As explained in the past, **growth stocks lost more during the correction, due to the fact that they have higher expected cash flows, which have to be discounted with a higher WACC (discount rate).**
- **If yields are falling, we have the reverse effect and therefore growth stocks should rise more than the rest of the market.**
- Mr. Ansidei is also posting the identical chart with source from Real Investment advice.



Source: Morgan Stanley via Mr. Tanase

Historical total return distribution for US bonds

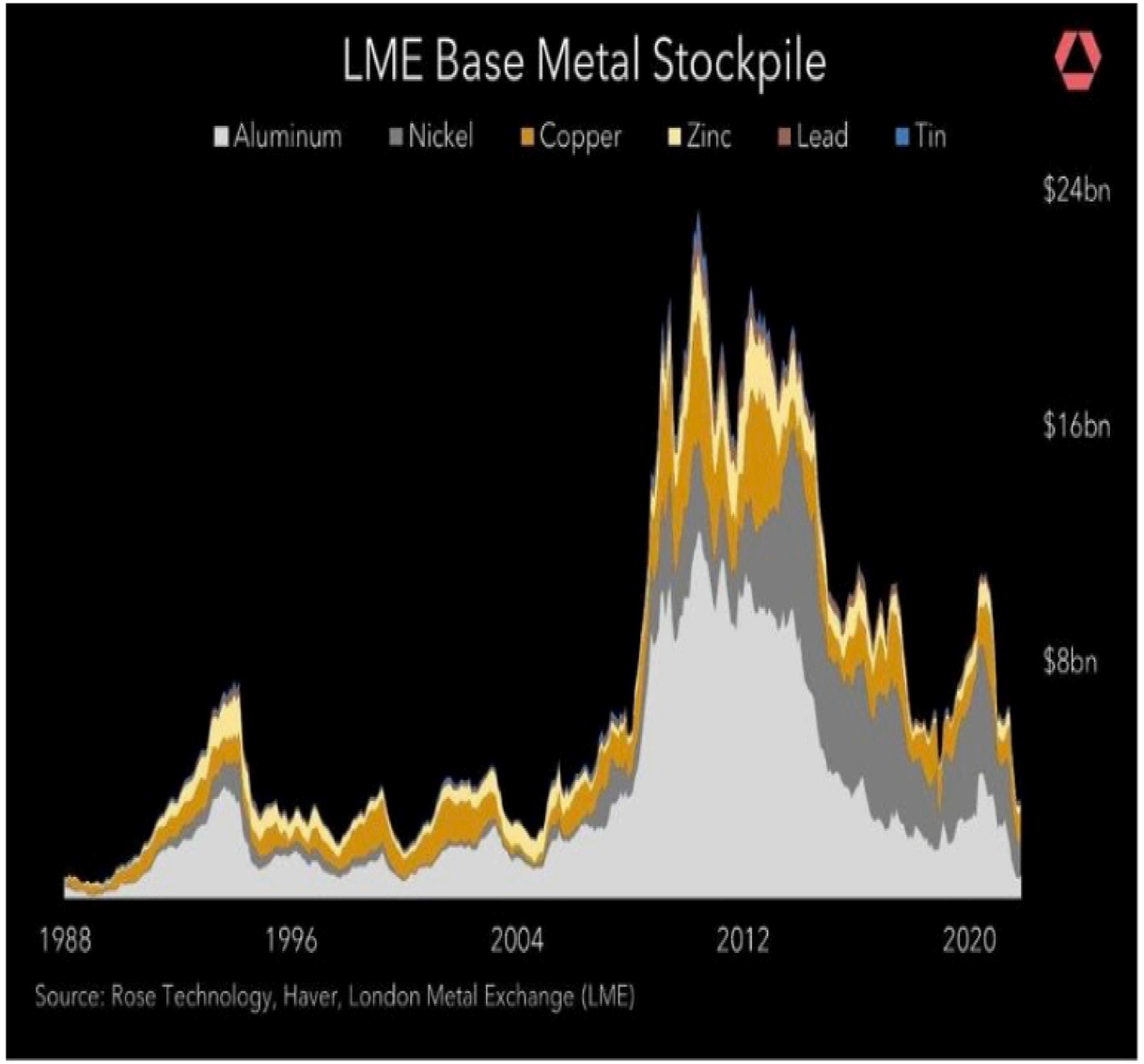
- We attach a very interesting chart, courtesy Mr. Zhao of Alpine Macro, showing the historical total return distribution for US bonds and we can notice, how 2022 historically has the most extreme negative performance ever.
- **Therefore, it is actually difficult to be negative also for 2023. The chart shows the distribution of returns over the last 150 years.**
- Historical, 2 years of negative returns appear to rarely follow each other (except for 1978/1979).
- Taking into account that KTS is expecting, as general consensus, inflation is going to fall significantly in 2023 and global central banks are already a pivot point, **we expect positive performances in the fixed income space for 2023 and therefore KTS increased the risk in the segment via the MAN high yield fund and European CLOs funds for the first time in the last 6 years. Those funds are highly liquid and therefore we can react immediately in case we have to change our base scenario.**



Extreme performance

LME base metals inventory are running very low

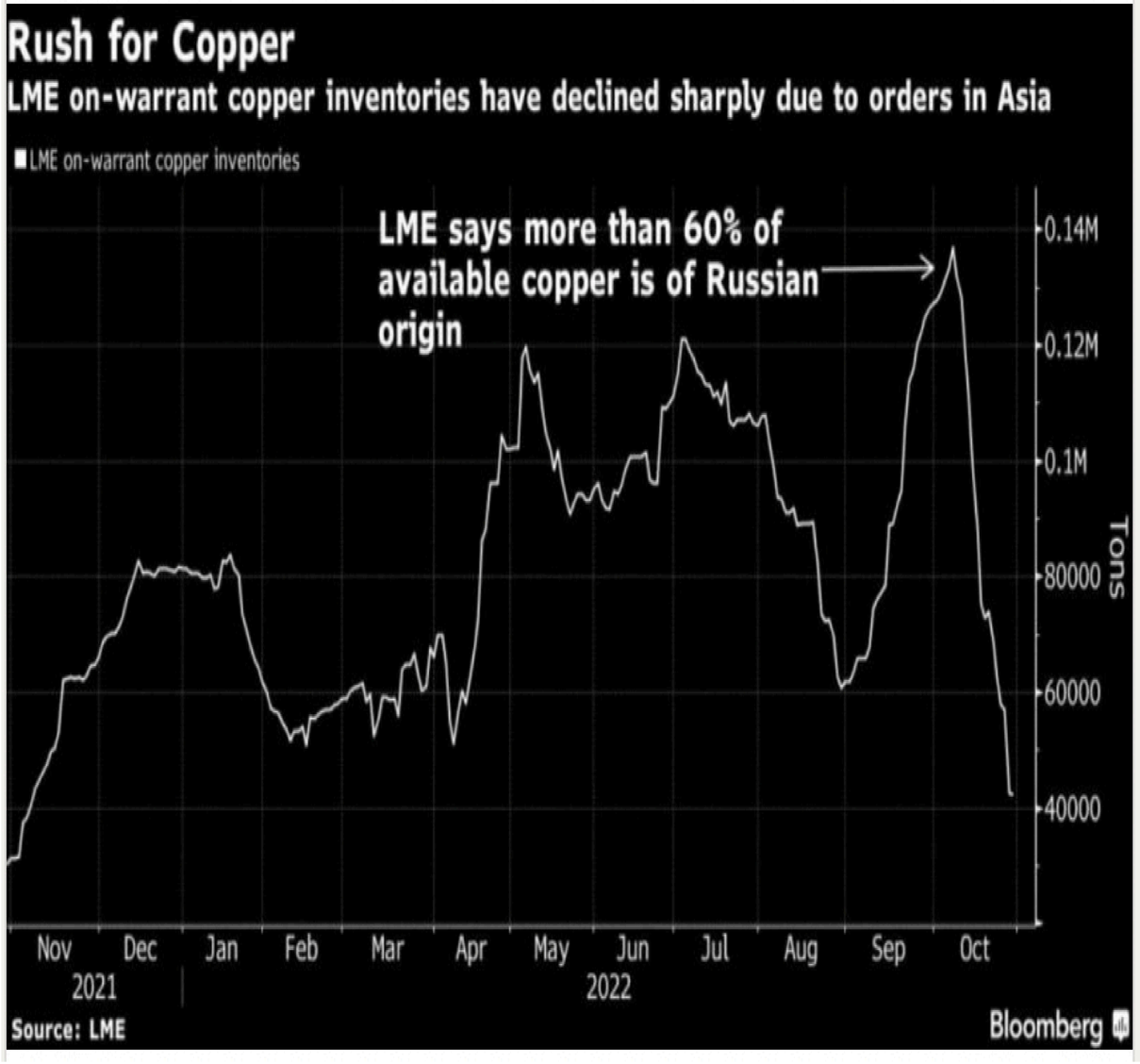
- On the right-hand chart we can notice, how **inventories for all metals are running very low at the LME** (not only, also COMEX and SHFE) and market participants are reminding the Nickel market squeeze a few months ago.
- Mr. Vogrinec argues in his latest blog, that the range of stocks in **official warehouses is just 3 days of global usage and we have never had such situation before.**
- The current situation is due to Chinese lock downs and if China recovers from lock downs, it could be tight for commodity markets, especially for copper.
- Therefore market participants see a bottom in copper price, in addition to the significant copper shortage on longer term, due to the green transition phase into EV, green energy, etc.
- KTS feel comfortable with our investments into our **best in class fund Bakersteel Electrum, Nevada copper, which could finalize the financial support from major shareholders and a few longer term investment like ZincX.**



Source: Wall Street Silver via Syz Group

Copper inventories

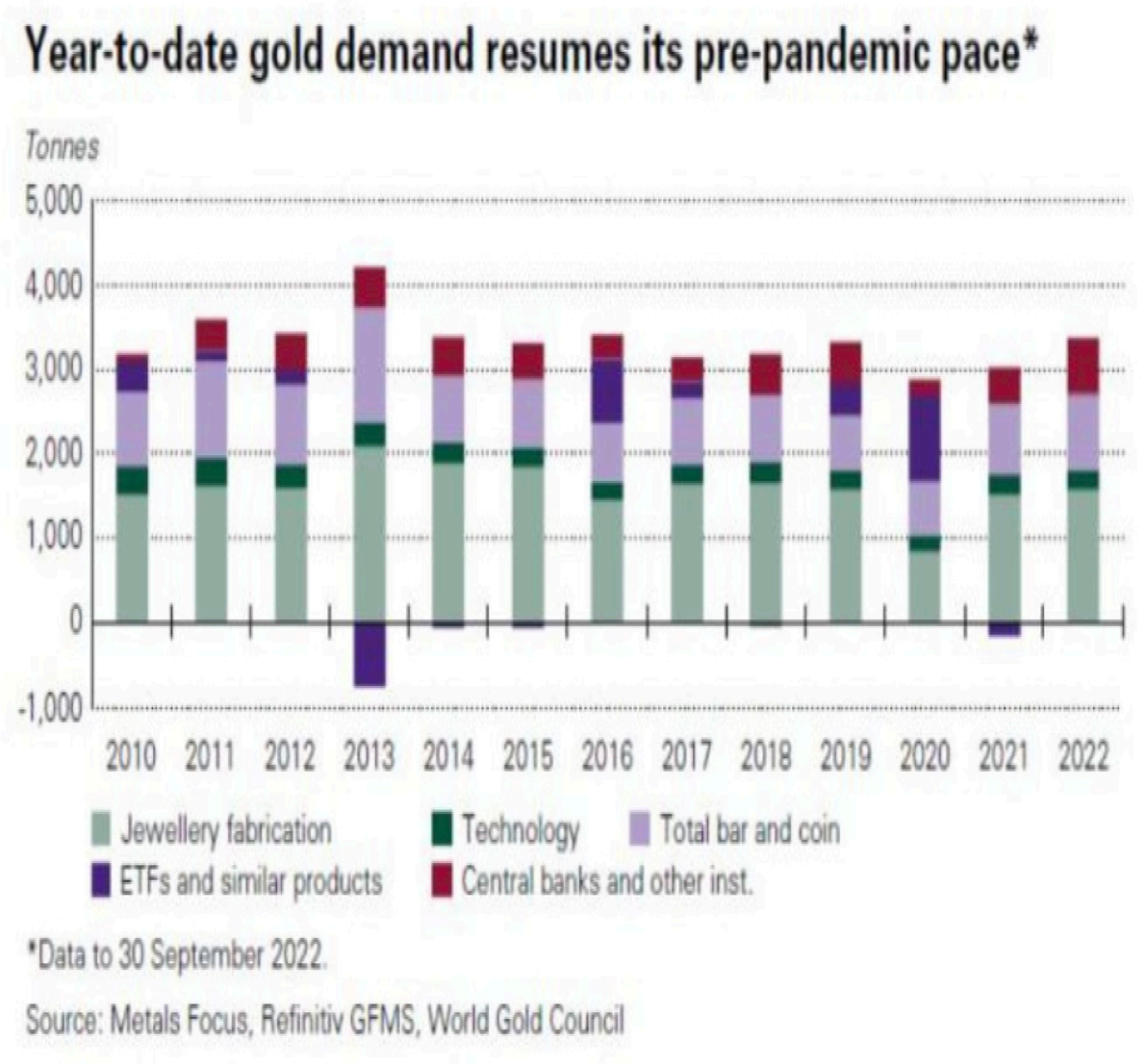
- We add the following chart, courtesy Mr. Vogrinect, where we can notice not only, that copper inventories are running very low, but LME says, more than **60% of available copper is of Russian origin.**
- If China is going to reopen the economy, there is a high risk, copper as other commodities could spike.
- We are not increasing our exposure, but some of our investments are basically like call options with no maturity on base metals.



Source: LME, Bloomberg via Mr. Vogrinec

Record Central bank buying lifts global gold demand

- The gold price is stable, but not rising.
- Meanwhile **global Central banks are buying gold and bought a record 399 tonnes of gold worth around USD 20 billion in the third quarter of 2022 alone.**
- The world's gold demand amounted to 1'181 tonnes in July-September, **up 28% from 922 in the same period in 2021.** Last year, the gold price was 1'800 USD, now around 1'650 USD.
- **Among large buyers were the central banks of Turkey, Uzbekistan, Qatar and India.**
- **There are other central banks, which bought substantial amount of gold but are not disclosing to publicity.**
- In a recent interview of the Dutch central bank Governor Mr. Knot, questioned about the possible insolvency of the Dutch central bank, Mr. Knot argues, **gold revaluation account is solvency backstop, and they are not going to sell gold.**
- **www.gainesvillecoins.com/blog/dutch-central-bank-says-**



Source: World Gold Council via Syz group

Brazil

- **Lula was elected as President of Brazil.**
- We are not going into politic, but it is insane, that an ex-President, who was convicted on charges of money laundering and corruption, of course in a controversial trial and sentenced to 9.5 years of prison, is now again President of the country.
- What happened to Petrobras, Vale and all the major companies in the country, we all know it and it is clear. There are enough proofs and funded documentaries on the subject, without mentioning all incriminated personality, which also were sentenced for prison.
- The fact that the **country is willing to go back to those times is alarming** and honestly we can not expect anything good for the economy and for international investors. We hope at least lower incomers will get a small part of the cake. Mr. Lula promised state investments, tax reforms and to end hunger.
- As history showed under Lula's government, the "corruption machine" was huge. Our energy expert is arguing that Mr. Lula may use again **Petrobras as a source of cash to finance the energy transition,** which would not be positive for shareholders. He was invested into Petrobras, which was a good investment up to today, but just sold it, arguing that on midterm, the plan could be good, but on the short term is negative for Petrobras.
- KTS tends to believe, as for China, that if an **investor wants to be exposed to a sustainable economy and invest according to ESG rules**, most probably Brazil would not be part of the strategy, unfortunately, because the country would have huge upside potential, possessing resources, having a growing young population and also demonstrated being a dynamic country.

Brazil

- We will monitor the situation and we were reading the latest research of our best-in-class fund Aubrey, which is not that negative on the potential of the country. The positive side of this election, is the fact, that the **congress is very divided and therefore it will be very difficult for Lula to push all of this policies through.**
- Alpine Macro argues, under Bolsonaro Brazil had structurally some important macro and institutional improvements in recent years and as a result the countries experienced a booming venture capital segment. With Mr. Lula as president, investors are asking themselves, how the future is going to be.
- Mr. Bolsonaro accepted losing and for a transition of power, therefore at least there is no political unrest and should help to ease the unrest on the street.

General news

- A good article in the blog finews.ch is rightly arguing as KTS was warning recently, **in Switzerland pension funds risks are not in the fixed income, but rather in real estate.** We can only hope, that the SNB is aware of this fact and is not going to provoke a collapse of the Swiss real estate market.
- Links to the article: https://www.finews.ch/news/finanzplatz/53943-pensionskassen-wer-sich-mit-hebelprodukten-verspekuliert?utm_source=linkedin&utm_medium=social&utm_campaign=dlvr.it
- The whole world is pointing the finger to the strict surveillance in China, but **The Netherlands wants to monitor all payments from 100 EUR** and this is going to open the door to unprecedented mass surveillance. This is possible only because of blockchain technology and is in preparation for the impending rollout of the fully programmable digital EUR.

General news - oil

- Also on the fact that **Biden's administration want to force the oil&gas industry to intensive investments into production and refining capacity,** shows how at the moment, governments are getting more authoritarian also in the West, not only in China.
- On one hand, it is right to stimulate investments and increase capex, instead of only apply for share buyback programs and honestly speaking, an increase in capex would be positive for the industry and the global economy, especially if canalized into alternative energies.
- But having the government threatening higher taxes to reach a goal, is unhealthy for the future of a "free economy". Or we are not anymore in a free economy? And if you tax companies now when they are reaching high profits, you also have to keep a buffer, when the oil price fall below a level that is not sustainable for the business to make a profit. Then the system would provide a fair stability.
- Our energy expert argues, that if **Republicans win, it would be good for domestic oil, especially services companies and pipelines** and the **best is yet to come for oil equities, which are 50% cheap vs historical measures at this stage of the cycle and especially cheap in Europe, given a 50% underperformance vs US peers YTD.**
- Republicans would not be good news for renewables, but most of green equities are back to 2018's levels and lost over 70% from their 2021 peaks.

General news on Asia and China: China could exit Covid zero policy

- At the beginning of the week, we were reading that apparently on social media there are videos, **showing 200k employees leaving the Foxconn Technology's manufacture on Covid19 measures**. This would be again a supply disruption for Apple. Bloomberg hasn't verified the authenticity of the content. Market participants are arguing, that rising tensions at Foxconn's Zhengzhou plant underscore the economic and social costs of Mr. Xi Jinping's Covid Zero policy, a **rigorously policed system of mass testing and lockdowns,** that has fostered growing resentment and it shows once again, the **potential risk to global supply chains and products from China's approach.**
- Based on this information, KTS would argue that the **longer China sticks on the Zero Covid policy, the more it will be isolated.** We have recently seen, that **companies are moving out of China to India and Vietnam and for this reason**, **KTS stays more focused on those countries,** rather than bet on cheap valuations in China, which are attempting, but we have seen in our last weekly report, after the speech of the Chinese President at the 20th National Congress of Chinese Communist Party (CCP), China is going to focus on security, rather than economy, and this is not giving a reassuring future for the country, **on the contrary sounds like more repression.** We let the main selection to our best-in-class manager, like Aubrey.
- But Mr. Peccatiello writes on his latest blog, there are **rumors, that China has formed a committee to assess strategies to exit the Covid Zero policy and reopen the economy** (source Bloomberg, HolgerZ)**.** Mr. Peccatiello rightly argues, if true, this is a big change for global macro conditions. Hong Kong stock exchange jumped on the 1st November +7.8%
- If China reopens, it should produce a non-inflationary growth boost and this would be very supportive for risk assets.
- Chinese authorities have conservatively expanded credit creation over 2022, but 40% of GDP-worth cities were in lockdown, and there fore, the Chinese GDP growth was modest. A total reopen would be a different story.

General news on Asia and China

- In addition, a reopening would sort out some of the residual supply bottlenecks in the global economy and hence marginally alleviating supply-side inflationary pressures.
- But also KTS would argue, a full operational Chinese economy would mean also increasing commodities prices, as also oil and therefore inflationary pressure for Western economies.
- **Anyhow, we would expect an initial positive reaction of global equity markets, which would strong support the ongoing year's end rally.**
- Meanwhile, Germany instead of decouple the relationship with China, is deepening economic ties. In fact, Mr. Scholz is allowing the Chinese shipping company Cosco to take a minority share in parts of Hamburg's container port. Apparently, there was a strong opposition from his own government according to the newspaper Financial Times. It is clear that the Chinese market is simply too big to be ignored, having many large German companies deeply invested in China and generating large shares of their profits there.
- Chinese are also expanding in Thailand and the company BYD Co., China's biggest maker of electric and hybrid cars, announced plans to build its first overseas electric passenger car plant in Rayong, southeast of Bangkok. More Chinese companies and private individual are moving to Thailand and it is not a coincidence, that the Thai government has just passed a new law, allowing foreign people or companies to buy land.

The real reason Elon Musk bought Twitter

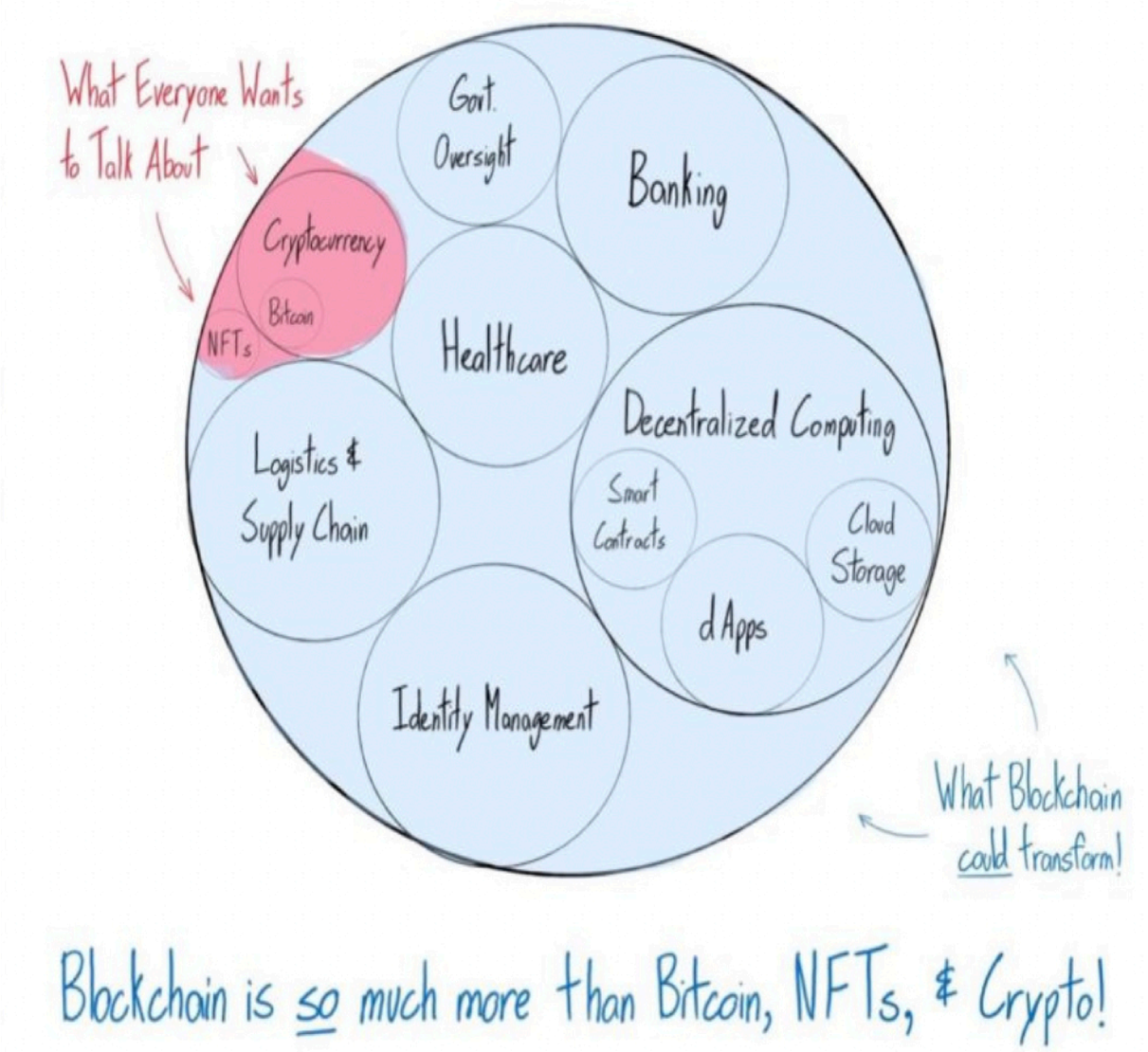
- Some blockchain's experts believe Elon Musk bought Twitter in order to build the next giant payment platform and they compared the project as the reincarnation of Libra, the payment project of Facebook, which failed, not getting the approval from authorities.
- As everyone knows, Mr. Musk was one of the founder of PayPal and at that time in 1999, the company was in a position to disrupt the payments business because of a new technology, the internet, and the maverick attitude of its executive team.
- Analyzing the new team in Twitter, Mr. Musk brought in Mr. Changpeng Zhao, Binance founder, Mr. David Sacks, who is ex Paypal and deeply involved in crypto and finally Mr. Sriram Krishnan, who invests for a16z Crypto and who has an Ethereum address in his Twitter handle.
- For this reason, experts do not believe in a political and media operation, rather in a new payment platform.
- According to an investor document obtained by the New York Times, Musk has predicted Twitter will bring in USD 1.2 billion in payment revenues by 2028 and therefore making the platform less dependent on advertisers.

ESG

- According to VP research, in **Japan the ESG fund labels basically disappeared,** after global regulators are introducing more rules to crack down on greenwashing by self-labeled ESG funds. In the last 5 months, no new fund has put “ESG” in its name, a sharp drop from roughly one a month for the past few years. Products still identify themselves as “green” or “impact” or “sustainable”, but since the Financial Services Agency signaled new regulations on ESG-labeled funds, asset managers have stopped using the shorthand for environmental, social and governance.
- Singapore and Hong Kong have both mandated extra disclosure requirements.
- In Europe, where sustainable investing is more formally regulated, asset managers are just getting to grips with new true-to-label rules that will result in hundreds of funds downgraded from the strictest ESG category to a less stringent one.

Blockchain's use cases

- We would like to attach the following chart, because a picture is worth a thousand words.
- Mr. Monserrat argues in his blog, that comparing blockchain vs crypto is like to say, the crude oil is only used to fuel your car. We like the comparison and it is was KTS always argued:
- Blockchain is the pillar for future development, from fintech to autonomous cars, digital health, etc.
- KTS feels comfortable with the exposure in the segment via different VC funds.



Source: Mr. Monserrat

DISCLAIMER

This report has been prepared by KTS Capital Management AG (“KTS”) / VICTRIX AG (“VICTRIX”) and is intended for information purposes only and does not constitute an offer or an invitation by, or on behalf of, KTS/VICTRIX to make any investments. Opinions and comments reflect the current view of The Investment Team of KTS/VICTRIX and not that one of a third party. We assumes no obligation to ensure that other such publications are brought to the attention of any recipient of this publication. Investments in the asset classes mentioned in this publication may not be suitable for all recipients. This publication has been prepared without taking into account of the objectives, financial situation or needs of any particular investor. Before entering into a transaction, the investor should consider the suitability of the transaction to his individual circumstances and objectives. This publication does not constitute investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate for individual circumstances, or otherwise constitutes a personal recommendation for any specific investor. We recommends that investors assess the specific financial risks as well as legal, regulatory, credit, tax and accounting consequences with a professional advisor. The information and data herein are obtained from sources believed to be reliable but no guarantee can be made that the information is accurate or complete.