KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 50

The 16th of December 2022

FOMC - perception of a too hawkish tone again

- After the good news of falling US CPI numbers and equity markets experiencing a strong short squeeze move the 13th December, on the 15th December, because of the hawkish tone of the FED, equity markets and gold corrected again strongly. We will go thought the US CPI and Powell's speech and will try to get some investment conclusions.
- **Powell's speech:**
  - The FED increased only 50 bps, which was expected, and most officials see rates ending between 5% and 5.5%, which is largely expected, even if many market participants are forecasting that the FED will be forced to reduce rates already from November 2023 due to recession and deflation! Basically markets believe that the FED is making a terrible mistake!
  - The problem is, market participants had the perception that the **FED is going to stay hawkish for longer,** especially after the Powell's assertions, "a restrictive policy stance likely needed for some time and will have to hold restrictive rates for sustained time", " need substantially more evidence of lower inflation" and finally "no rate cuts until confident inflation moving toward 2%". Most probably, having lower CPI numbers the previous day, most of investors were expecting a dovish tone, included KTS.
- **Economists agree that after the most intense FED tightening cycle in last 40 years, it is hard to believe that the economy will experience a soft landing, with the FED, but also the ECB, staying hawkish for longer time (chart not included, Mr. Trahan).**
- Mr. Fugnoli also argues that back in the 70s, there are multiple examples of how policy makers were pressuring the FED to change monetary policy, when the economy fell into recession. He also mentions that back in 2018-2019, when Mr. Powell was too hawkish, he had a confrontation with Mr. Trump, eventually Mr. Powell changed his monetary policy.

FOMC - is all about labor market

But Mr. Fugnoli also argues that for the Biden's administration, the year 2023 is the right year to "clean up" in order to be prepared for election year 2024 and therefore, most probably, will not pressure the FED.

- As we will see in slide 9, the market is not really believing the FED and expectations are in line with the 5%, but not higher.
- **Lisa Abramowicz tweet after the FED policy on the 14th December is interesting: The FED: we're hawkish! We have more work to do! The market: got it, so you're doing another step-down to a 25bp rate hike in February and will be cutting rates by later in the year. Got it"**
- **But Mr. Powell spent at least 8 minutes of the press conference endlessly repeating, how hot the labor market is.**
- Surprisingly, the FED still keeps its economic projections for a real GDP to grow by 0.5% in 2023, and 1.6% in 2024. As previously explained, no one believes it. Everyone expects now a recession.
- Reading reliable commentaries around, it is clear to everyone, after Powell's speech, that it will be impossible to keep rates over 5% for longer, without causing a recession. In addition, we are reading other good comments, arguing, that it is clear, the **structurally imbalanced labour market is caused by million of excess retirements during the pandemic** and KTS would also add, to not forget the 3.5 mio citizens, which are invalid after the pandemic. The FED acknowledges: "retirees do not appear to be returning to the labour force to increase the labour supply sufficiently" and therefore believes to restoring balance to the labour market with a moderation of labour demand, which is basically caused only with a recession. Do the Biden's administration really wants a recession in USA in 2023? Or it would be better to open up the U.S. Board with targeted immigration?
- It is a political discussion, which is not in the hands of KTS.

FOMC - economists and experts agree, the FED is doing a mistake

- **Mr. Bill Ackman tweeted, the FED 2% inflation target is no longer credible. De-globalization, the transition to alternative energy, the need to pay workers more, lower-risk, shorter supply chains are all inflationary. The FED cannot change its target now, but will likely do so in the future!**
- Mr. Fugnoli argues in his latest blog, that market participants are telling loud to the FED that it is not the right time to be extremely hawkish, when the world is in the midst of a war, the global economy is in slowdown, the debt vs GDP is at highs and therefore interest rates can not be over the GDP's growth. The ECB is in an even more dangerous situation, having peripheral countries like Italy in financial distress.
- Other more pessimistic experts argue, and fundamentals are clearly pointing out, that the FED could be dovish, but after the FED and ECB speech, it is clear they are not and therefore it is too early to take any risk adding equities.

FOMC - conclusion

- The FED asserts that the labor market is hot. But KTS was analyzing, that it is not, and in the **next months, numbers will collapse due to massive layoff of major companies**. Mr. Peccatiello is also asserting that **forward-looking labor market indicators show US non-farm payrolls are likely to slow to 0 by March next year and turn even negative.**
- In addition, we have seen, financial conditions and banks lending standards have tightened very aggressively in 2022, and they lead hiring patterns by 9 months, which of course are going to be massively lower than today.
- Mr. Peccatiello argues, that the **FED has never hiked their FED funds rate past the level of 2y Treasury yields.** After the hike of 50 bps, rates would be at the same level as 2y T Bills. Therefore any additional hike in 2023 will push us through uncharted territory from this point of view, and with the **FED funds rate above 5%, the FED will lead the US into a recession.**
- As previously explained, the bond market does not believe the FED, and believes that there is no way the FED can go over 5% or keep 5% for the entire 2023. Credit Suisse argues that the FED will not go over 5%, but will stay for longer at 5%. Nevertheless, CS is positive for equities and bonds in 2023, getting the market accustom with central banks policy.
- Traders are expecting **YoY CPI to fall from 7.5% today to 2.5% in only 8 months** and Mr. Peccatiello asserts, historically this can happen only with a serious recession. For this reason, he is still not advising to buy risky assets.
- Finally, Mr. Ackman argues to change the 2% inflation mandate, but the **FED make clear, changing the inflation target is not something we are thinking about under any circumstances. Our inflation target is 2%**
- The sad joke of the day: Powell is basically saying: keep calm, I just want you to lose your jobs!
- Other investors argue, even evidences are for holding rate hikes, it is **now all about credibility.**

ECB, SNB and BoE

- The Swiss central bank hiked interest rates by 50 bps. We have now a rate of 1% with a predicted inflation of 2.4% in 2023. The SNB Balance sheet is also falling, and therefore there is less liquidity for equity markets. We believe, the SNB just followed the steps of the major central banks, but the **strong CHF does not give much more room of maneuver.** We believe, the CHF is too strong for the Swiss economy. On one way, Swiss citizens are enjoying lower inflation than other countries, but exports are the most important part of the Swiss economy.
- We believe that the analysis of Mr. Peccatiello on the ECB is the most accurate one. The ECB had 3 main points:
  - The foreseen core inflation is 4.2% by December 2023, and therefore double of the 2% target
  - Ms. Lagarde announced that the **ECB is going to hike more than market participants expect**
  - QT is going to start in Q1 2023 with 15 bn per month and higher in Q2. The balance sheet is actually already shrinking fast (300 billion in a few months) due to TLTRO repayments from banks and will also continue next year.
  - The 3% terminal rate must be priced much higher, the **ECB wants to bring nominal rates above the level of core inflation. Market was expecting a rate below 3% before the meeting and inflation expectation are at 4.2%**
  - Therefore much higher 2y yields, should bring higher long-end yields, which is translated also in a flatter yield curve (Mr. Peccatiello expects -100 bps). Basically it make sense to invest in longer EUR maturities.
  - **Italian bonds under trouble, will have a repricing on higher risk-free rate, but also spreads widening.**
- What the ECB communicated is even worst than the FED, and is not promising; on the contrary, **market participants are now expecting the European economy to fall into recession with a too hawkish ECB.**

US CPI - finally also the core inflation lower

- US inflation came at 7.1% , expected 7.3%, therefore slightly lower and market participants welcomed the news on the 13th of December.
- **We would like to point out that all economists from major investment banks were expecting higher numbers and only Mr. Larsen was expecting 7.1%. Therefore, it turned out that the constant analysis of indicators by Mr. Larsen is working very well.** KTS likes the macro analysis of Mr. Larsen, which is quite in line with our forecasts.
- The core inflation came also lower (-0.5% m/m), while finally the rise in the price of core services remained unchanged at 6.8% y/y.
- Core goods, **especially Covid sensitive items, as used care, car rentals, airline fare, TV, toys and PC** fell by 3% m/m and core services is essentially a story about rents (40% of core CPI). Market participants are still expecting rents to continue rising in Q1 2023, but analyzing the slide nr. 12, we believe that the **news of a new calculation on the OER was almost unnoticed.**
- Finally, the share of small business, which is planning price hikes was unchanged in Nov at 34%, but still largely above long-term average. On top, only 44% of small business owners have open jobs (down from 51% in May), but still very high.

US CPI - food inflation due to bird flu and extreme heat

- By analyzing food prices, which are keeping soaring, we can notice that **eggs are up 49.1%, butter and margarine 34.2%, bread 15.7%, milk 14.7%, coffee 14.6% and chicken 12% with an overall increase of 12%.**
- By imputing in google, why eggs prices are so high, CNBC explains, that the **dynamic is primarily due to a severe outbreak of bird flu in the U.S.**, which has killed many egg-laying hens but has largely left chickens raised for meat production unscathed, according to economists. The bird flu is actually a known phenomenon through the whole 2022.

https://www.cnbc.com/2022/11/11/why-egg-prices-are-surging-but-chicken-prices-are-falling.html

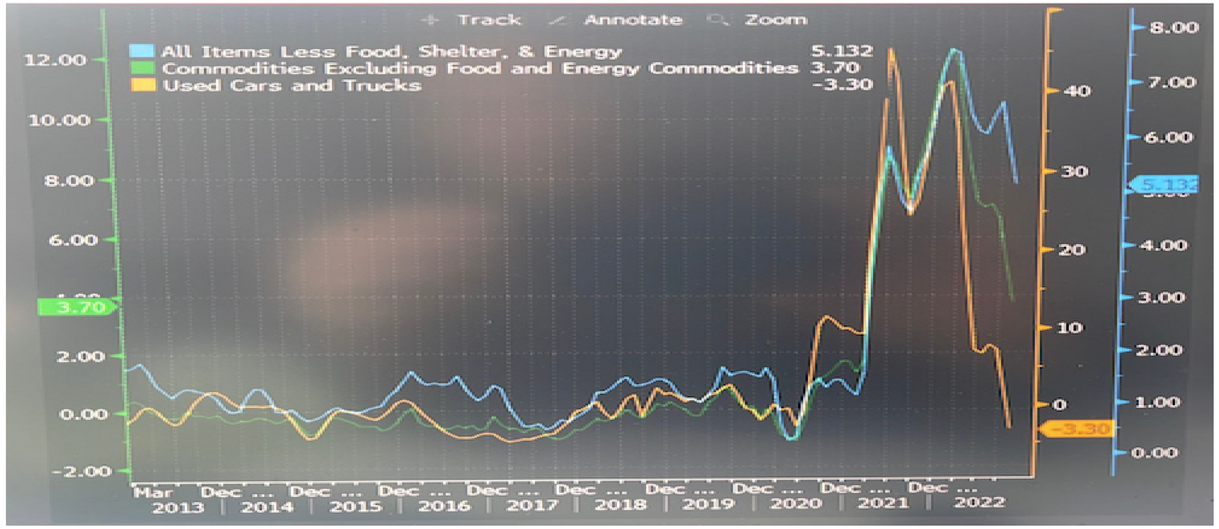
- On butter, margarine and milk, apparently prices hit an all-time high partly because **extreme heat is taking a toll on diary cows**.

https://www.marketwatch.com/story/butter-prices-are-at-an-all-time-high-partly-because-extreme-heat-is-taking-a-terrible-toll-on-dairy-cows-11664386592

- **It is actually clear that having the FED constantly increasing rates, is not going to help to take down the price of eggs or milk!** Those are special situations and we are wondering why no one mentions such subject.
- On the sticky food inflation, if we analyze the Q3 2022 result of Nestle, which still have a 9% price's increase, **most probably we will see a slowdown only in Q1 2023.** But even if Mr. Peccatiello asserts on his latest blog, that even the stickiest components of the **CPI basket (ex-housing) are coming down aggressively now, which is, of course, positive.**

US CPI - we are in deflation in some goods

- On the left-hand chart we can notice, how the price in some segments are collapsing and even in deflationary territory.
- On the right-hand chart, courtesy Mr. Larsen, the **CPI basket ex housing is already in deflationary territory** and Mr. Larsen wage to assert, that economists should start to worry about deflation for H1-2023, rather than inflation as everyone does, included the FED.

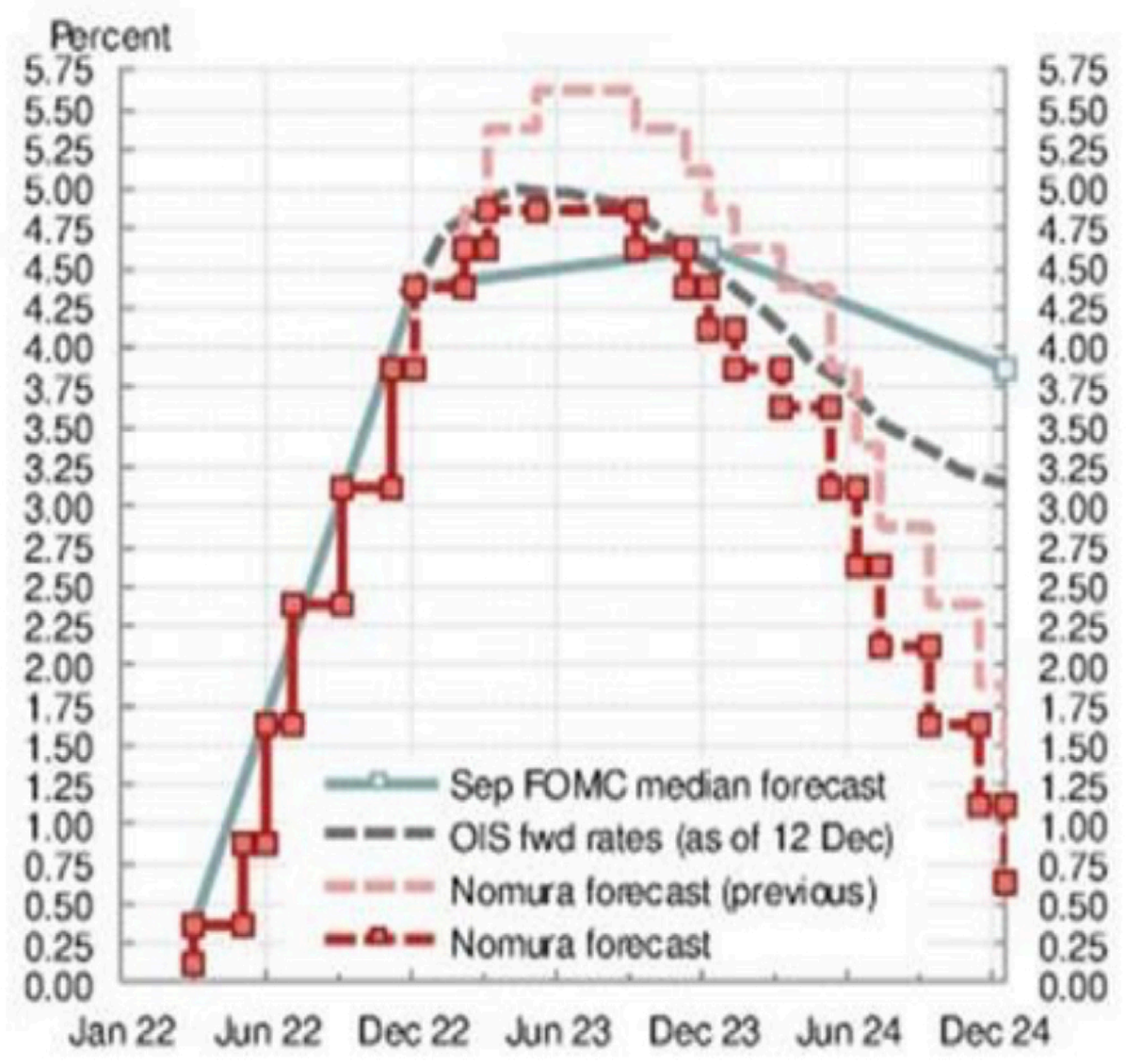


Deflation in used cars, 40% lower energy prices, and shipping costs fell

Deflation (Source: Macrobond via Mr. Larsen)

Expectations for the FED's policy rate

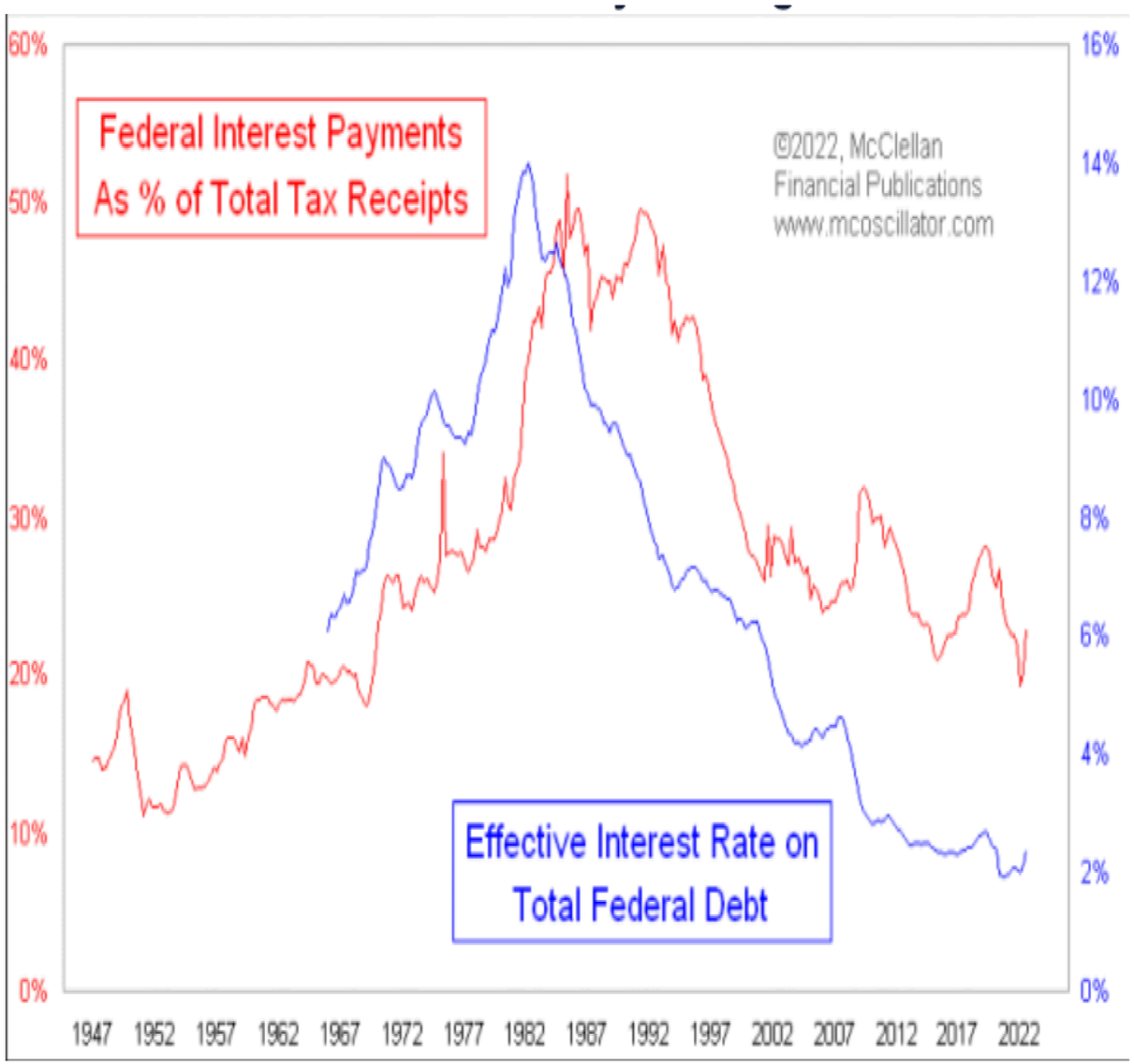
- Mr. Nicholson, CIO of Nomura, argues that the FED has been super hawkish for some time, but the continued deceleration in monthly core CPI inflation during November suggest that the FED will likely pause rate hikes earlier than assumed.
- The problem will be the core **PCE inflation in January, which will likely rebound, due to the increase in healthcare service prices.**
- Nevertheless, analyzing FED's rate expectations, it is quite clear that the majority is believing that the **FED is going to pause in March and the increase is not higher than 5% by March 2023.**
- The big dilemma is the current elevated wage growth and core services, which remain strong, but according to our analysis, will eventually start falling as well.
- **Meanwhile we are reading today, Goldman Sachs is planning to cup up to 8% (!) of its employees in January.**



Expectations are a pause of rate hikes in March and falling from November

U.S. Federal government is not ready for high rates

- On his latest research, McClellan argues that the **total US federal debt has risen in every year since the 1950s.**
- It even rose during the supposed budget surpluses back in 1999-2000.
- U.S., but not only, having a **high debt and not even more increasing interest rate, is a unsustainable burden.**
- In the chart we can analyze, back in 1981, the total federal debt only amounted to 31% of GDP, the lowest point of the last few decades. Under FED Chairman Paul Volcker, the cost of paying interest increase to 50% of total tax receipts.
- **Afterwards, thanks to lower interest rates, interest costs fell to 5% of GDP.**
- With a current debt 120% of GDP, if interest rates would go up to 10.4%, every tax dollar collect, would be just enough for paying debt service. Not being able to cut taxes, a high tax collection in % of GDP is not good for equity. **So bottom line, the USA can not afford higher interest rates!**



Source: McClellan

US CPI - market's reaction

- On the 14th December due to lower US CPI, we could experienced the perfect scenario, indicating what could happen in 2023:
  - Equity markets higher, due to a short squeeze
  - USD lower, forecasting lower inflation and therefore lower interest rates
  - Gold higher, due to lower yields
  - Bond's yields lower, therefore higher bond prices
  - A lower USD is good for gold, but also for Emerging markets
- We would like to add, that on the 12th December the **put options ratio increased at the highest level ever as also the premium paid for puts vs calls (USD 4.2 in put options for every USD 1 in call options, which is the double what they spent during all the other panics over the past 22 years, chart not included)**, therefore many investors were hedging ahead of CPI numbers, which came lower than expected. **Such behavior is for KTS a sign of capitulation.**
- We will see on slide 22, that market participants are also speculating with 24h option contracts, not having high convictions.
- On the 15th December we had the exactly opposite reaction, having market participants worrying about the hawkishness of central banks
- **We would expect a stabilization of equity markets up to year's end, being the end of the tax selling's period and still having share buyback programs ongoing. The first 2 weeks of January should be positive due to the usual pension funds inflows into equities. Thereafter we will have to decide, if we should reduce some tactical positions and increase our liquidity for trading opportunities.**

Major changes in the calculation of US CPI

- A fact, that was almost unnoticed, is the constant methodology changes by the BLS for the calculation of the CPI Index.
- We can notice, that back in May 2022, the BLS started changing the methodology on new vehicles.
- But most importantly, from January 2023, the **weighting of OER** is going to change and of course, needless to say, such **new methodology will depress inflation** and therefore KTS feels even more comfortable, that in **2023 US CPI is going to fall further and the FED will pivot.**
- We sense that everything is perfectly coordinated in order to dismiss pressure on the FED, in order to get more dovish, which should help stabilize the economy and avoid a recession; actually a perfect scenario for equity markets.
- Of course we agree with market participants like Mr. Trahan, that since 1980 all the changes made were supposedly done to depress CPI, which helps the job of the FED, but not the general population, which is losing purchasing power.

Consumer Price Index

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Recent and upcoming methodology changes: 2022

Owner's Equivalent Rent (OER) Unit Weight Refinement (*posted September 2, 2022*)

Beginning with January 2023 data, BLS plans to adjust the weighting method for Owner's Equivalent Rent (OER) in the CPI. The new method will use neighborhood level information on housing structure types to weight OER's unit sample observations. BLS will continue to sample and weight housing units to be geographically representative. In some neighborhoods, detached houses are underrepresented in survey responses so additional unit weight will be given to underrepresented detached houses in the OER index sample. For more information on adjusting housing weights for structure types, see the research article "Location, Location, Structure Type: Rent Divergence within Neighborhoods."

January 2023 CPI weight update (*posted May 24, 2022*)

Starting with January 2023 data, the BLS plans to update weights annually for the Consumer Price Index based on a single calendar year of data, using consumer expenditure data from 2021. This reflects a change from prior practice of updating weights biennially using two years of expenditure data.

Changes to new vehicles source data and methodology *(posted January 13, 2022)*

With the release of April 2022 data in May 2022, the CPI program plans to replace the data collected by the BLS for the **new vehicles** index with transaction data from J.D. Power. This index will continue to include prices for cars and trucks, but will no longer include motorcycle prices. Two special relative series that are currently published, **new cars** and **new trucks**, will also now be based on J.D. Power data. Publication of the combined **new cars and trucks** series will be discontinued at the same time. The full list of discontinued series is available online.

Seasonally adjusted indexes and calculated seasonal adjustment factors will continue to use BLS collected data, and will not take the new data source or methodology into account until the year 2023. Revised indexes and seasonal factors are available at Seasonal Adjustment in the CPI.

The Measuring Price Change in the CPI: Research new vehicle methodology factsheet is planned to be updated once this change takes effect. Research and the methodology leading to these changes are described in detail in a working paper: "A New Vehicles Transaction Price Index: Offsetting the Effects of Price Discrimination and Product Cycle Bias with a Year-Over-Year Index."

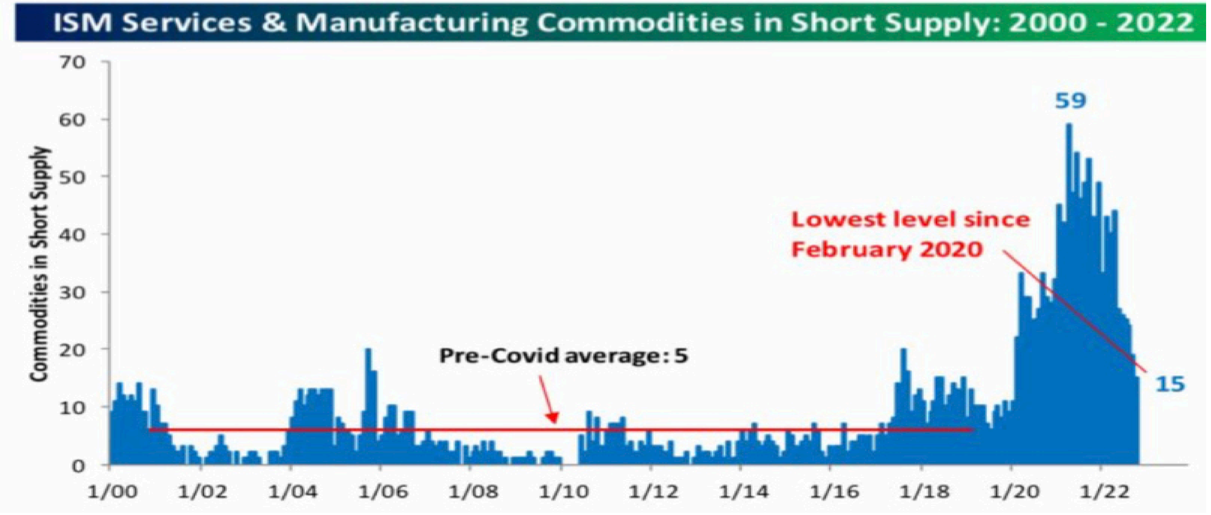
For archived recent and upcoming methodology changes since 2017, see the recent and upcoming methodology change notice archive.

Last Modified Date: August 29, 2022

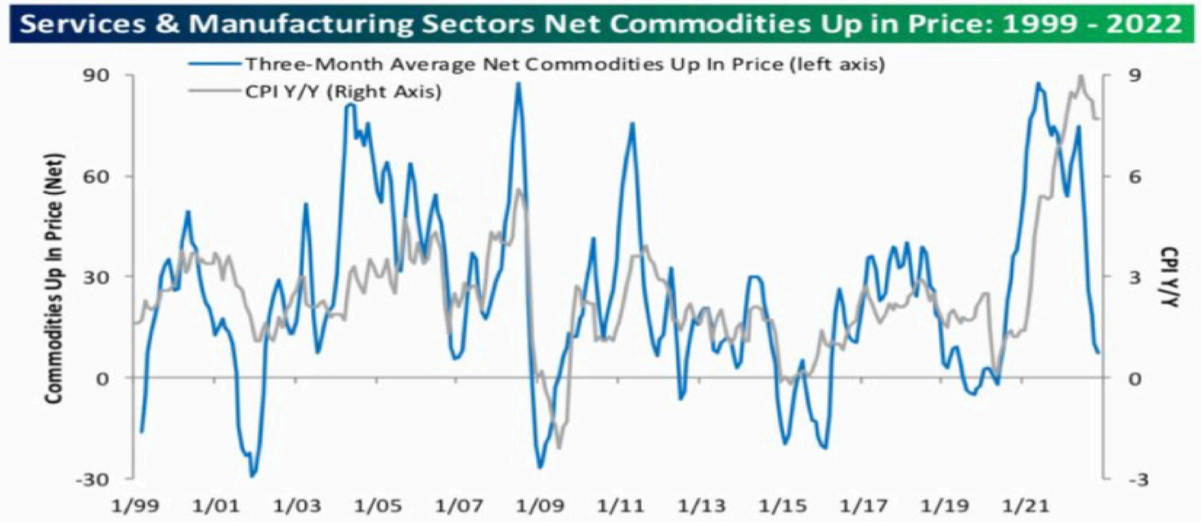
Source BLS.GOV

Fundamental signals pointing out a lower inflation

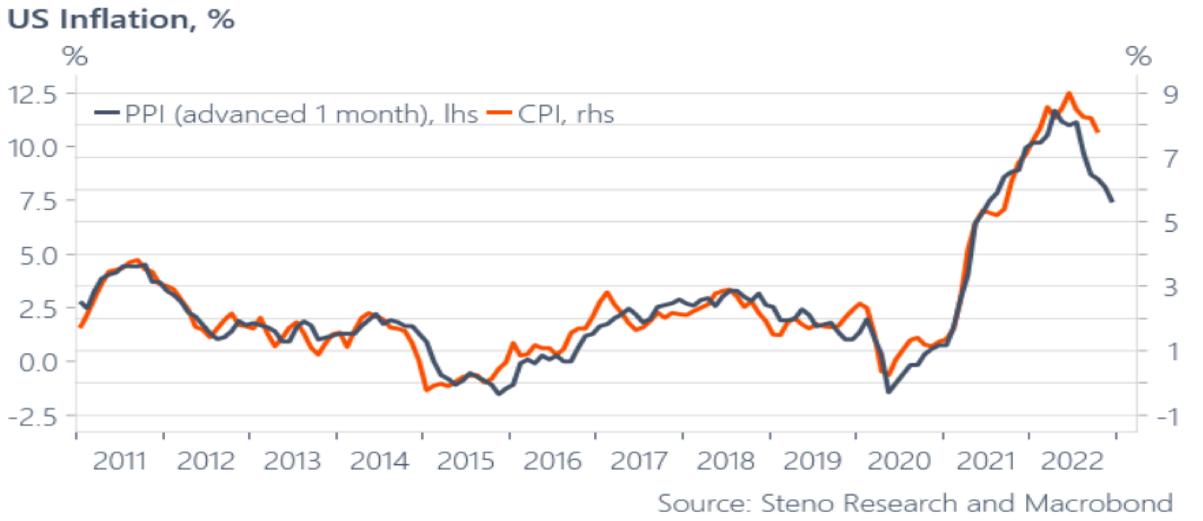
- Last week the investor community was worrying about slightly higher PPI. Mr. Budelmann argues that other signs continue to point to lower inflation ahead.
- The monthly **ISM survey shows falling commodities prices** (a basket of 17 commodities).
- In addition, the number of commodities reported as being in short supply has also plunged. November's net level of 15 was still triple than pre-Covid average of 5, but is down sharply from a peak of 59, to its lowest level since February 2020.



The number of commodities in short supply also falling



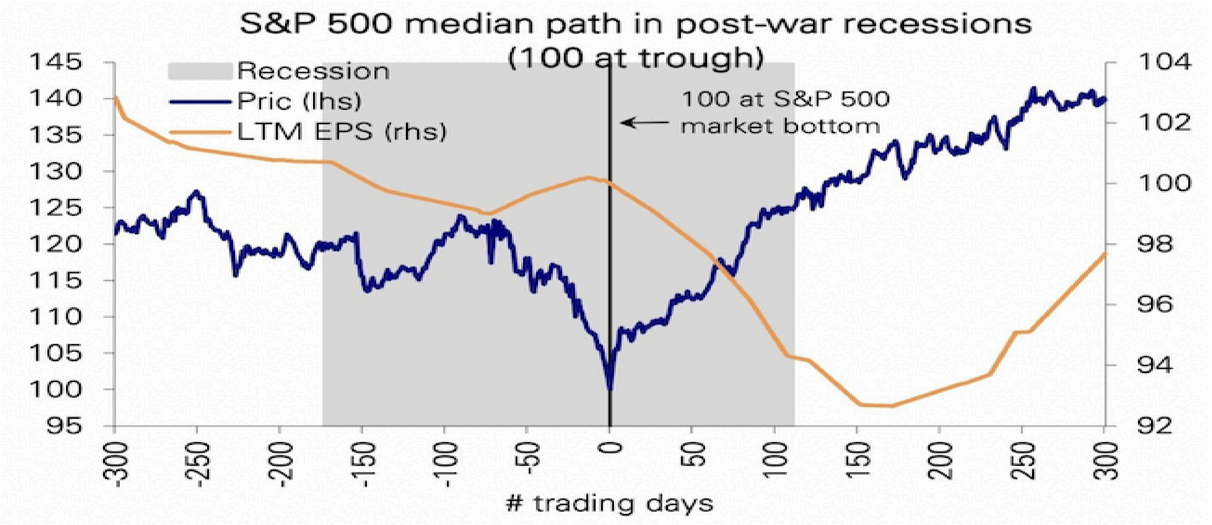
Commodities prices falling, so should CPI



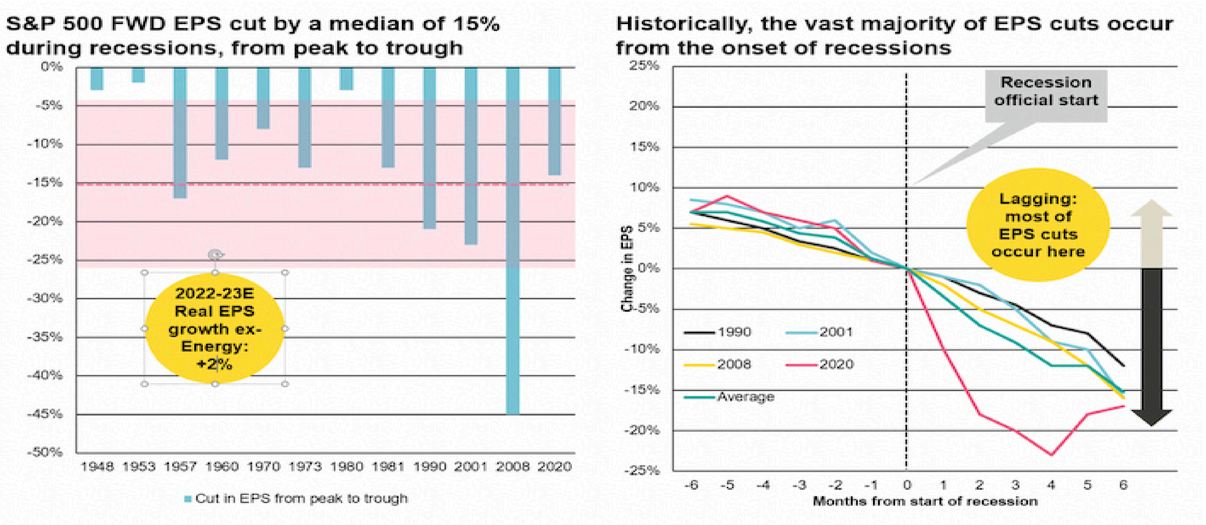
Mr. Steno Larsen: CPI headed below 6% soon

Equity markets typically bottom half-way through a recession

- Deutsche Bank is arguing in a similar way, as Vontobel recently did, that equity markets are **typically bottom half-way through a recession, but earnings typically bottom only after the recession has ended** (left-hand chart).
- Mr. Mario Montagnani, senior investment strategist at Vontobel, posted again the chart showing, that **equity markets anticipate recession on average 7-8 months before their official start (NBER) and the average earnings cut is 15% from peak to through, most of which is after the recession is made official, therefore lagging.**



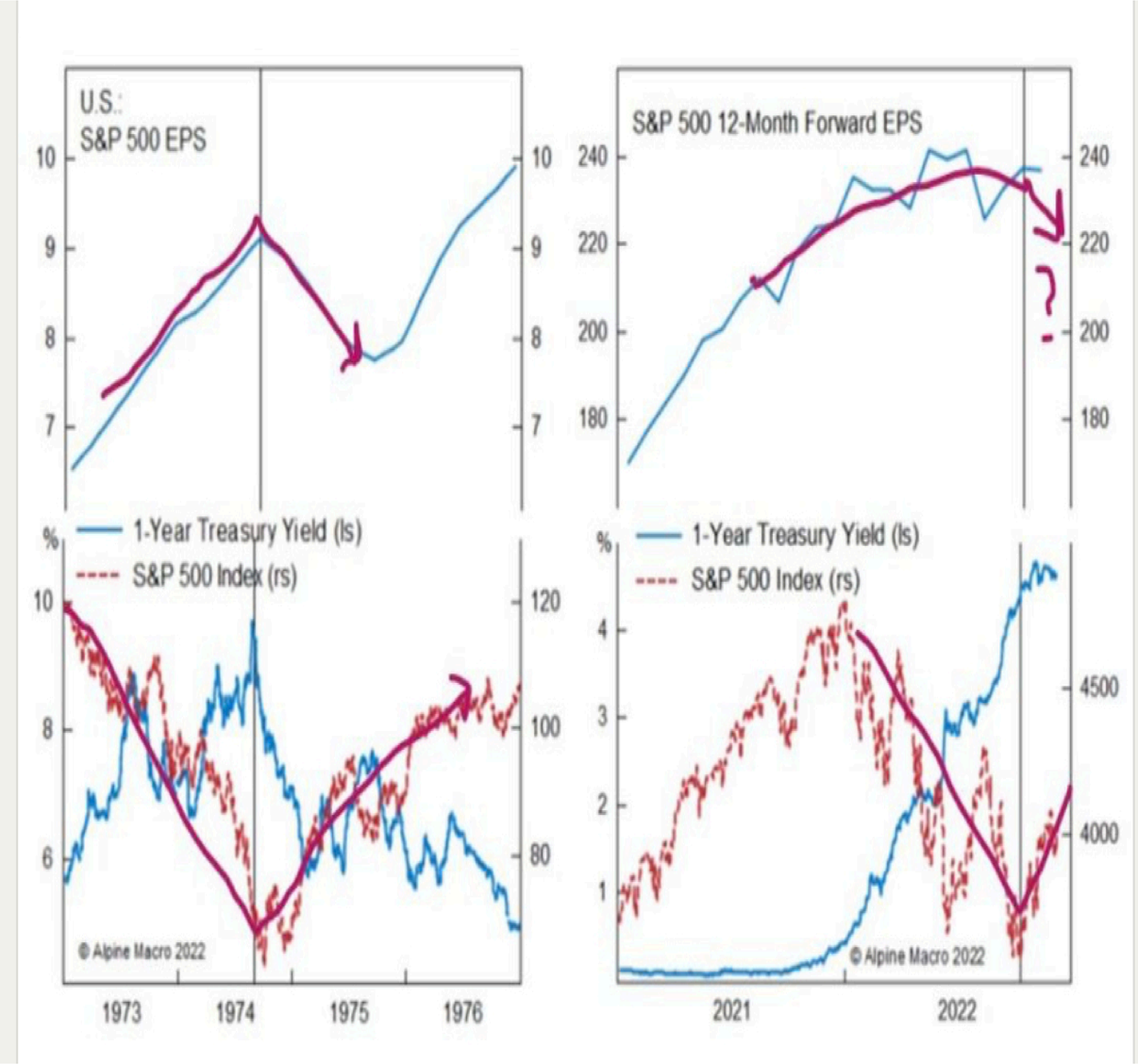
DB: equity bottom earlier than earnings



Source: Vontobel

1974 - U.S. Equities bottomed out when both interest rates and EPS peaked out

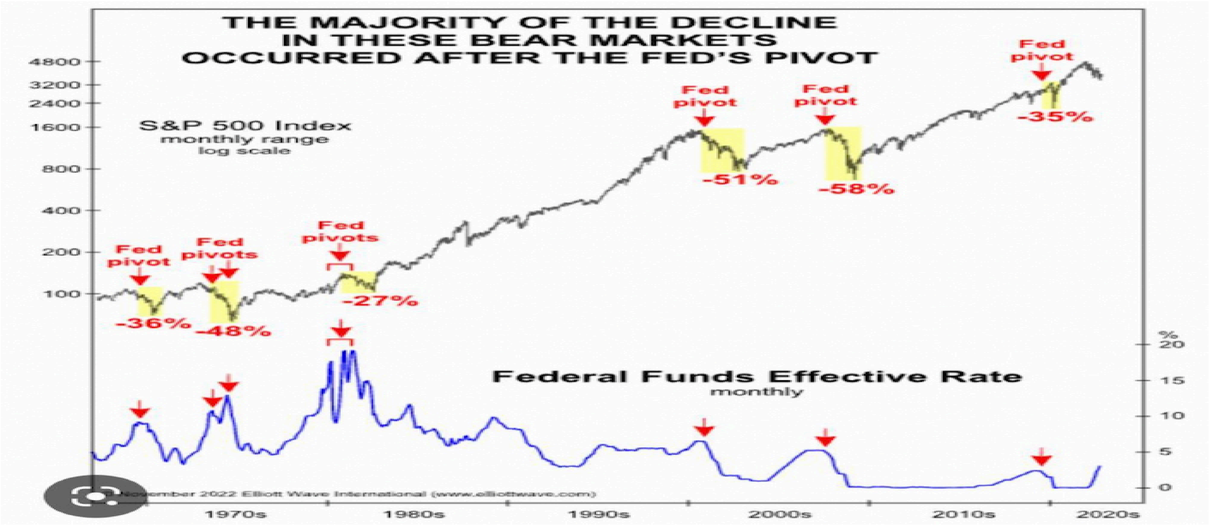
- We include the right-hand charts, which are also confirming slide 13.
- We can analyze, that in 1974, **U.S. equities bottomed precisely when both interest rates and EPS peaked out, and this was followed by a sustained recovery in prices even though corporate earnings were falling into a recession.**
- Why was so, because interest rates started to fall, investors tend to look beyond the immediate valley in earnings and to discount a better economy ahead and therefore Mr. Zhao rightly ask, if 2023 going to repeat 1974.
- Having the majority of professional investors strongly underweighted equities due to fears of recession next year, which will have negative repercussion on corporate earnings, the risk 1974 could repeat, is high.

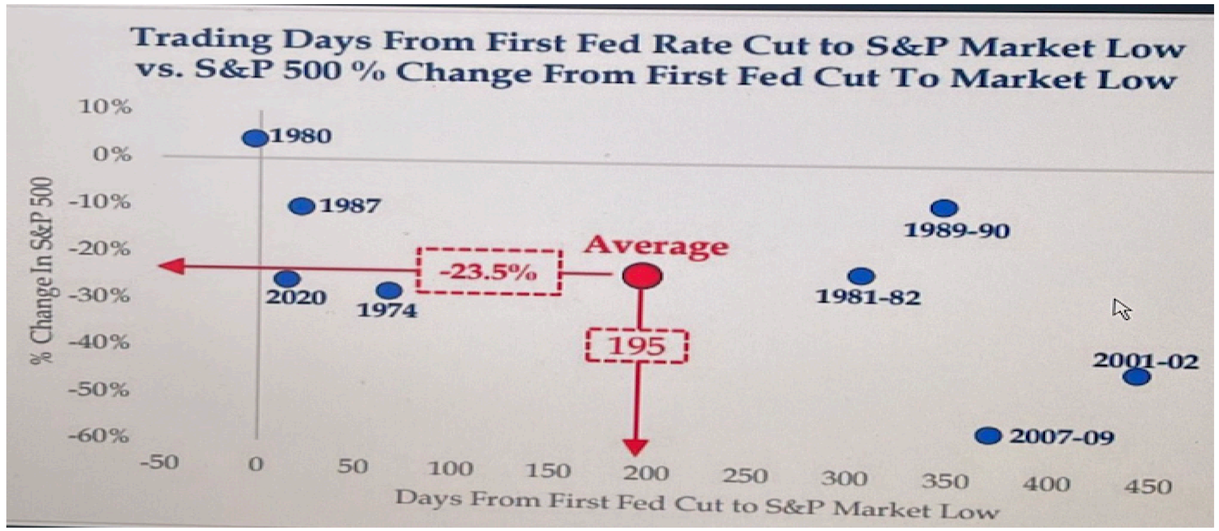


Source: Mr. Zhao of Alpine Macro

Chart on equity markets' correction after the FED's pivot

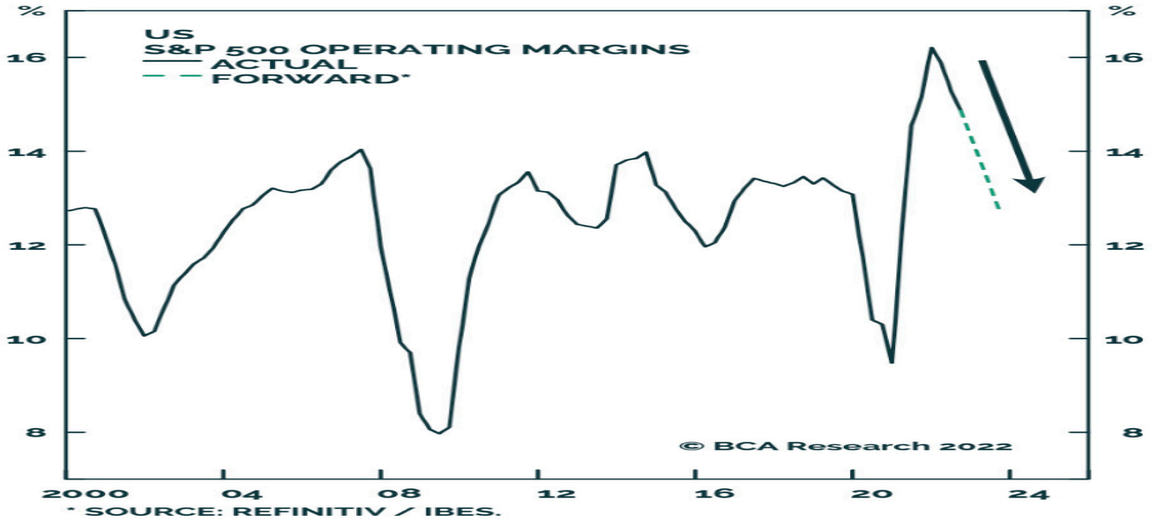
- Finally, for the reasons mentioned in the previous slides 13 & 14, we do not believe that the current situation is comparable to most of the past cases, because this time, equity markets are trying to discount the upcoming recession in 2023 and therefore already corrected, meanwhile the FED is still increasing interest rates.
- As we have recently analyzed, global CEO's are holding back investments and capex, as long as global central banks are changing monetary policy.
- On the contrary, in the past, the FED started reducing interest rates when the global economy was already falling into recession.



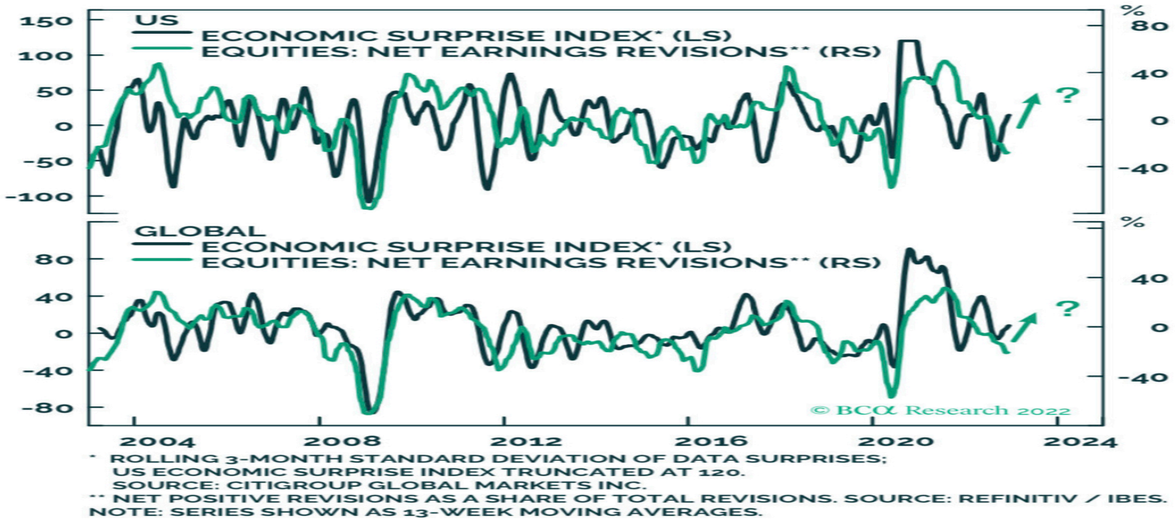


What is, in case growth surprises are on the upside?

- Mr. Berezin rightly pointing out, economic surprise indexes are stabilizing and even turning.
- Equity markets are discounting a fairly steep decline in profit margins and therefore, if growth would turn higher, profits could too.
- After the speech of the FED and ECB, we do not believe, CEOs' companies are going to react any time soon, on the contrary, will still hold back investments.
- We understand market participants holding back investments, because in order to change the sentiment, we need central banks to change monetary policies. KTS still believes that following fundamental data, everything is pointing out to a lower inflation and the peak of labor market. In addition, there is still the hope of the Biden's administration opening up border to target immigration and making pressure on the FED to do not push it too "hard".



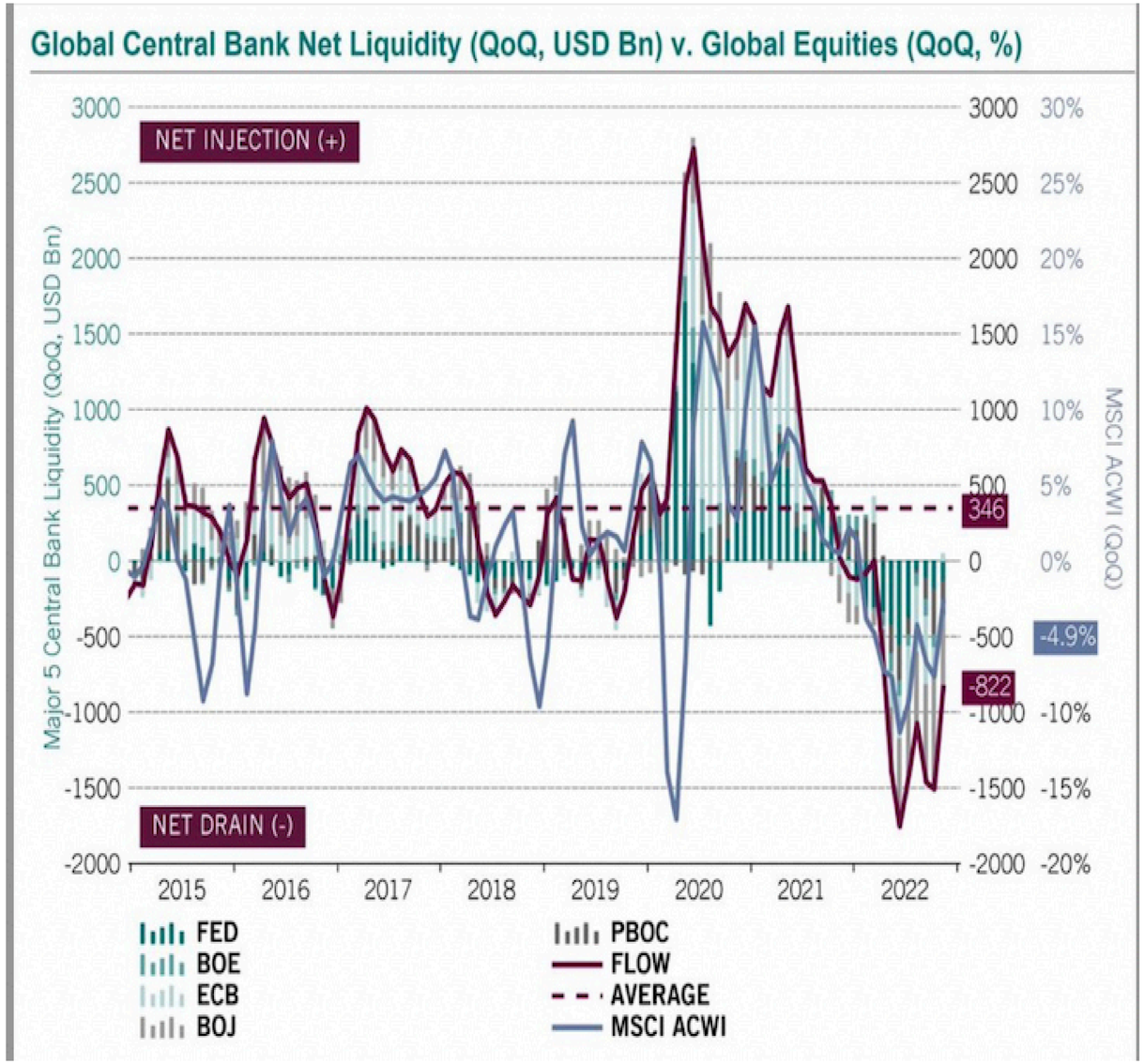
Equity markets are discounting a steep decline in profit margin



But economic surprise index are possibly turning higher

Improving central bank liquidity

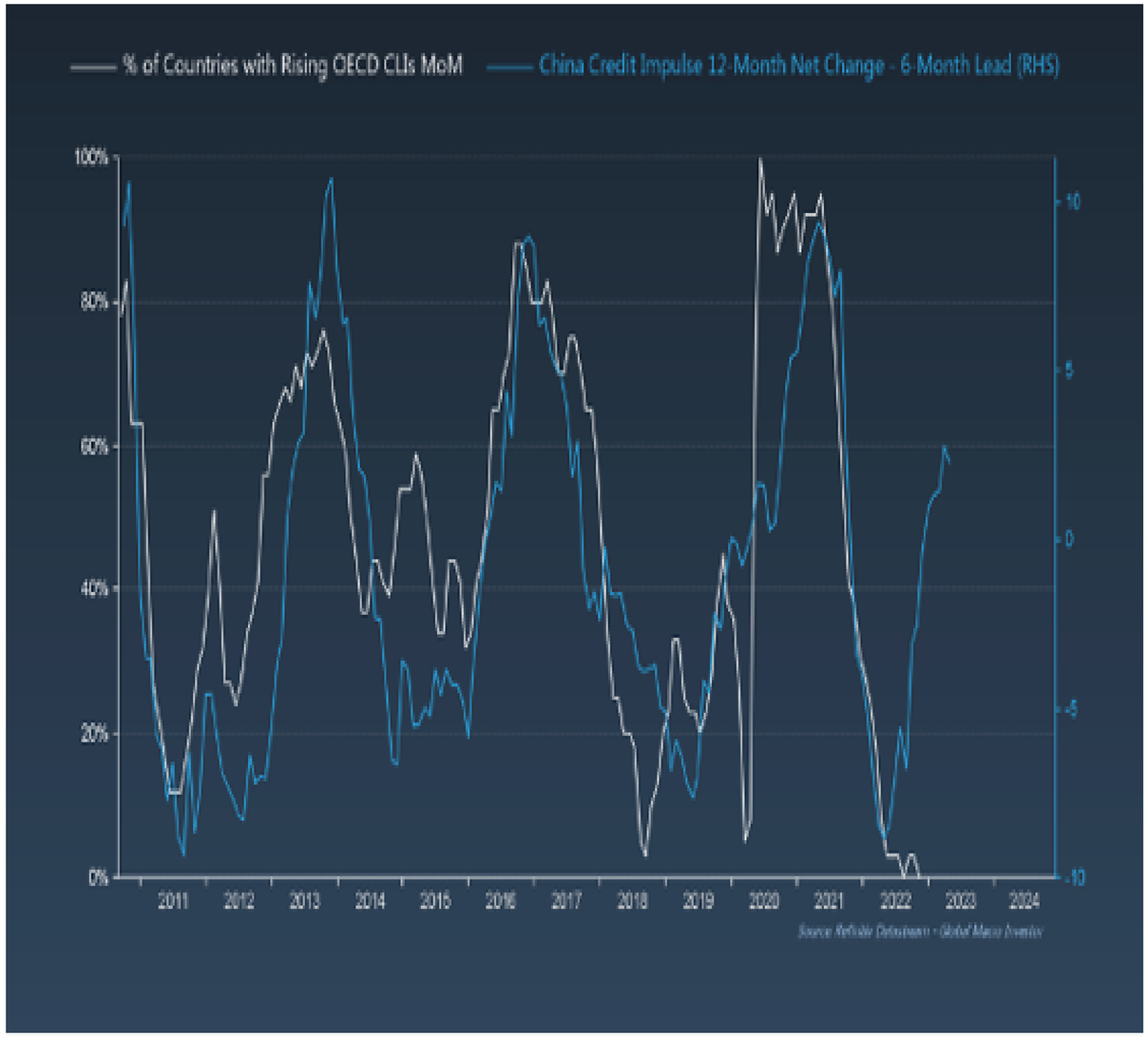
- We are posting an interesting chart, courtesy Mr. Rowles via Callum Thomas, showing that central banks' liquidity is improving.
- Mr. Pal argues in his latest blog, that there is most probably no discussion on the magnitude of the possible recession, with the ISM falling to 40, but the real question is the **duration of the recession.**
- According to Mr. Pal, **financial conditions are already as tight as during the Global financial crisis (with 4 standard deviations),** but inflationary pressures is starting to ease, with bond yields and USD also down and the peak of FED's hawkishness.
- Finally, credit spreads are not going to blow out like they did in 2008. As analyzed in the past, there are not macro imbalances comparable to GFC 2008 and the possible recession in 2023 is the result of soaring real yields and unprecedented tightening in financial conditions, but both can easily remedied with rate cuts and QE.



Picture Title

% Of countries with rising OECD CLIs MoM vs. China credit impulse

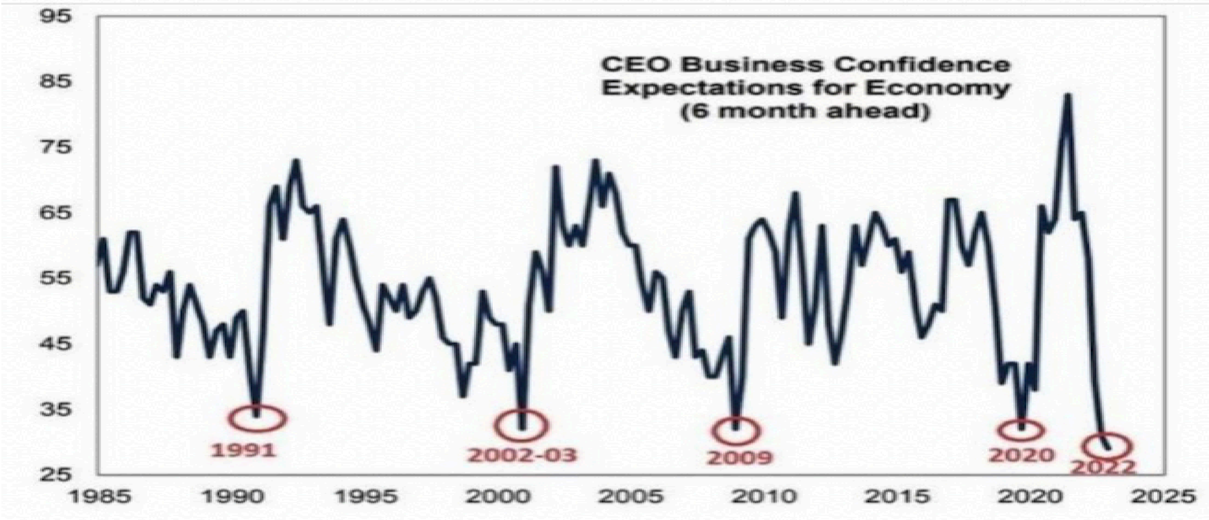
- Mr. Raoul Pal brought last week the subject of increasing M2, which is going to be the major trigger for 2023.
- **On this latest blog, Mr. Pal brings the right-hand chart, showing the improving Chinese liquidity conditions, which leads OECD country breadth by six months and therefore asserting that global growth momentum should soon bounce.**
- This is coming, with the US equity put/call ratio at highest levels in 20 year history and with the Philadelphia Fed survey probability of recession index over the coming 12 months at highest levels. Basically literally everyone sees the recession coming and officially, as already mentioned last week, is the most anticipated recession on record. Also Mr. Peccatiello shows a chart, where economists have never been as “worried” about a recession as today (historical data since 1975)!
- Meanwhile, analyzing the US investor intelligence survey net % bullish vs S&P500 Index, is at most bearish levels, indicating that everyone is positioned for lower equity markets.



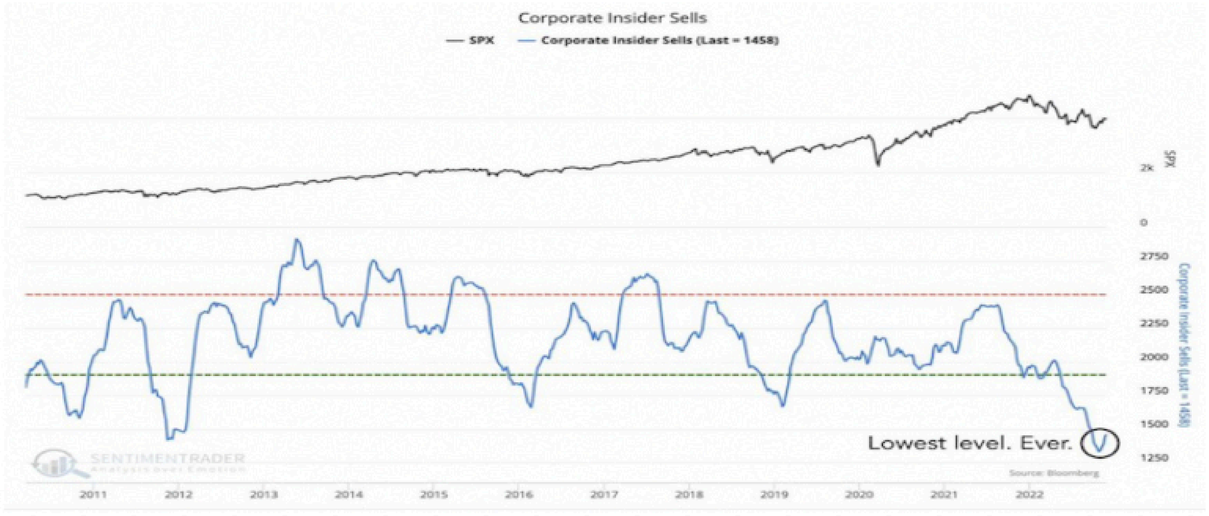
Picture Title

CEO sentiment at lowest level ever, but also insider selling

- We include again the charts, courtesy Mr. Monchau, where we can notice, that historically, the lowest **CEO business confidence coincides with the bottom of the equity market**.
- In addition, CEO sentiment is extremely depressed, but **insider are not selling anymore.**
- Finally, we believe, that the day, the **FED is at inflection point, and global central banks change monetary policy, global CEOs are getting more confident and start to invest again.**



Lowest levels in CEO confidence.....

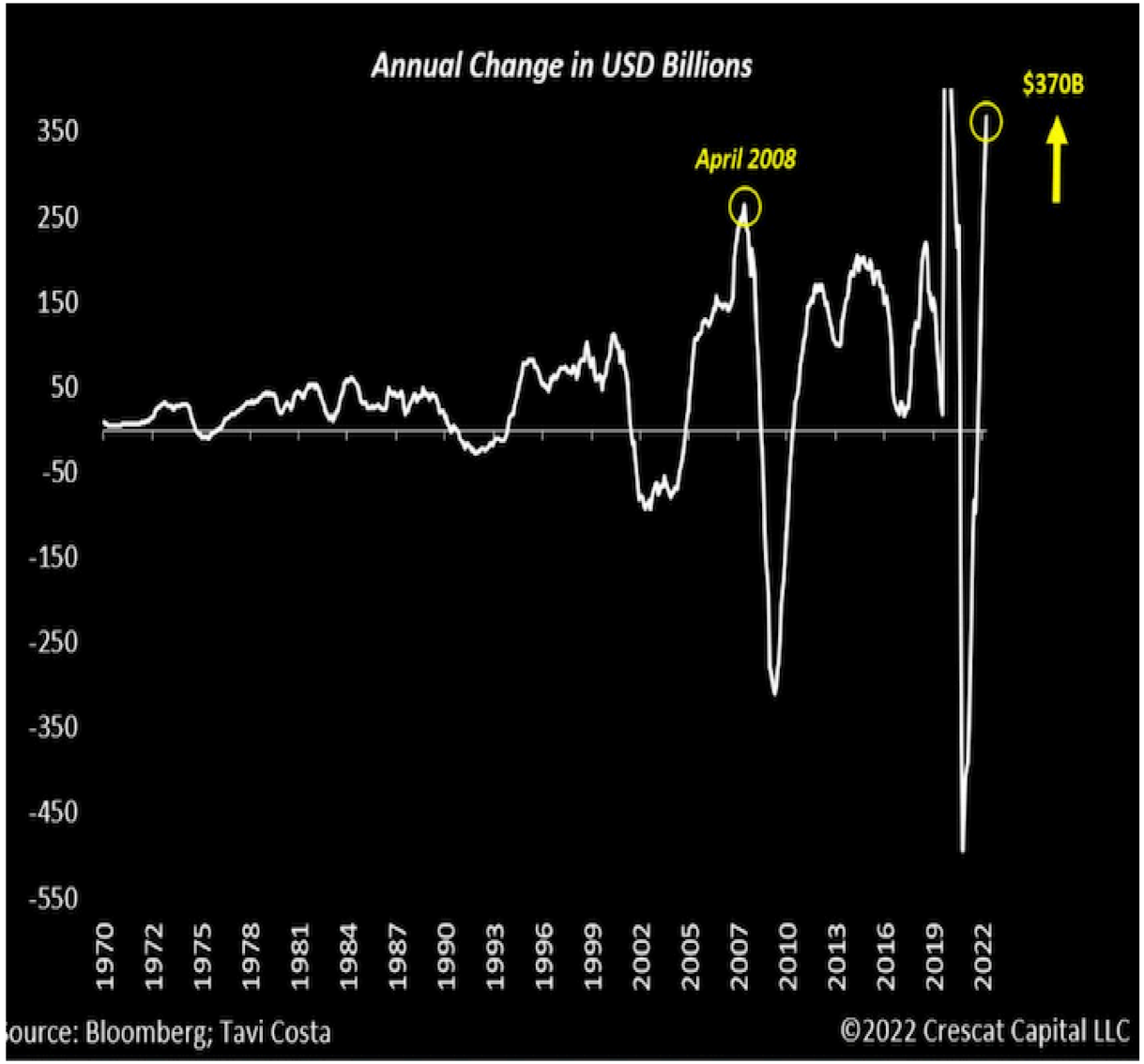


Insider selling at lowest level ever

Coincides with the bottom of equity markets

US commercial & industrial loans

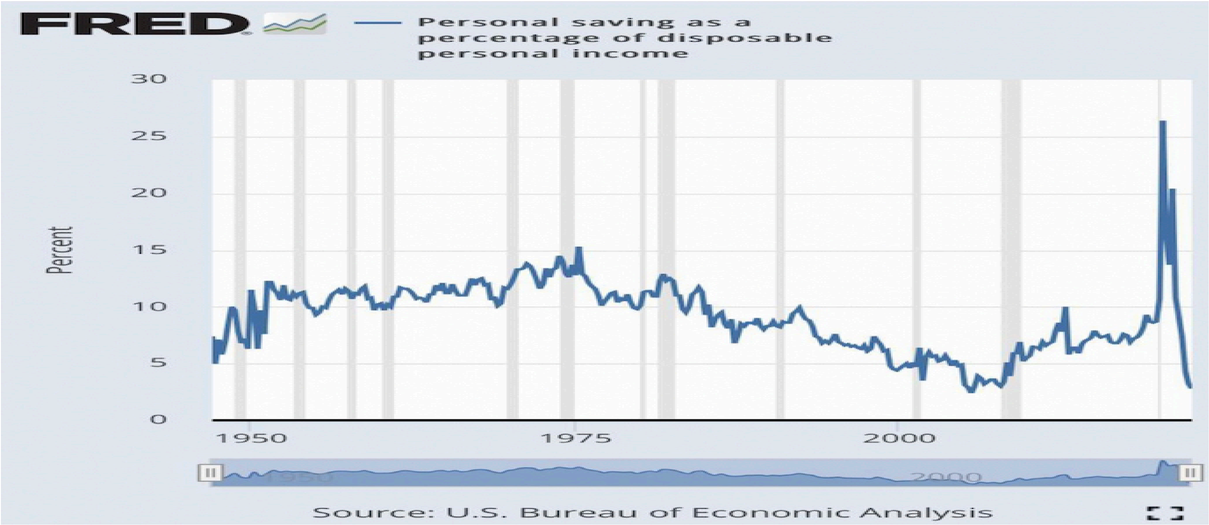
- Even if KTS believes, we should have a better development of the economy and equity markets in the year 2023, we have to be aware of possible structural financial distress.
- Mr. Costa is showing the chart of **US commercial & industrial loans, which increased by USD 370 billion in the last 12 months.**
- The last times this happened, were April 2008, just before GFC 2008 and during the pandemic.
- It means that **companies need liquidity in order to afford distressed times and the magnitude of the current loans requirement is definitely alarming.** There is still not a credit crisis, but if the current situation would be prolonged, there is definitely a higher risk.
- This is a reason to be invested in high yield bonds **only via external mangers with a solid track record and to keep a disciplined trading with stop loss.**



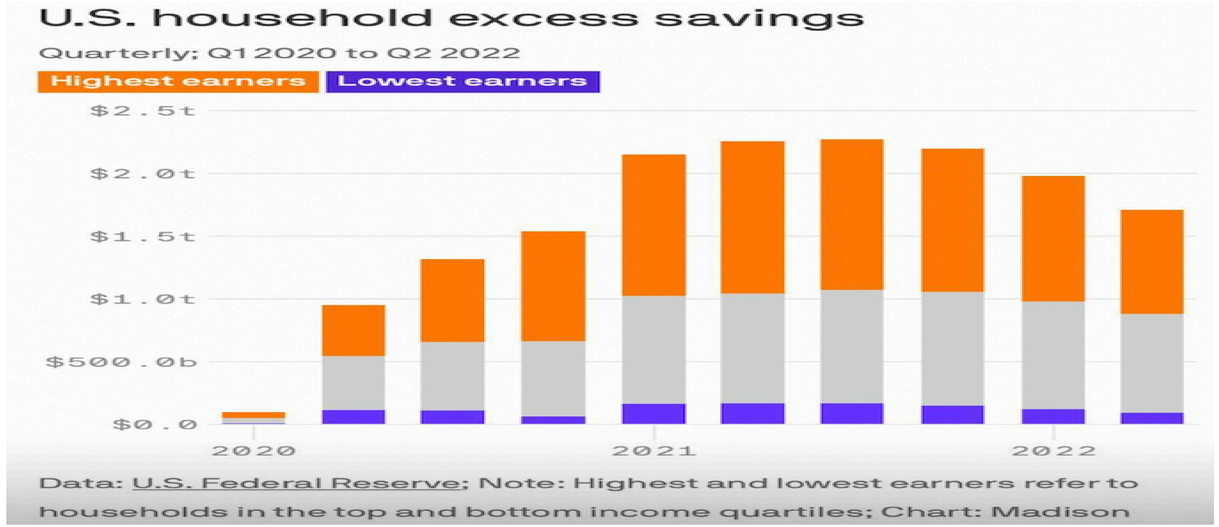
Source: Mr. Costa

Personal savings

- The main argument for many market participants, is a weaker US consumption in 2023, having personal savings collapsing. In fact, US consumers are using savings in order to compensate high inflation.
- **But the most important data to take into consideration is the fact that 50% of excess savings is in the hand of the highest earners, which are basically 70% of consumer spending.**
- **As we recently mentioned, KTS was surprised back in August, reading a survey of Saks Luxury Pulse, where high-income consumers answered, that they are not letting inflation and recession worries change shopping habits.**
- We include the links: https://www.retailcustomerexperience.com/articles/high-income-consumers-not-letting-inflation-recession-worries-change-shopping-habits/



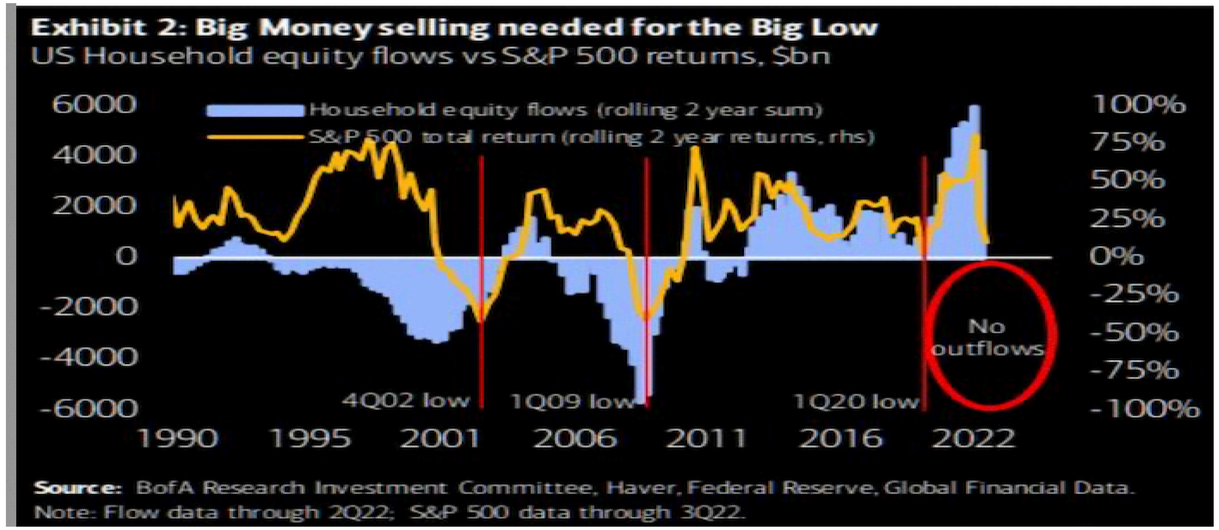
Long term personal savings: still over USD 1.5 trillion ?



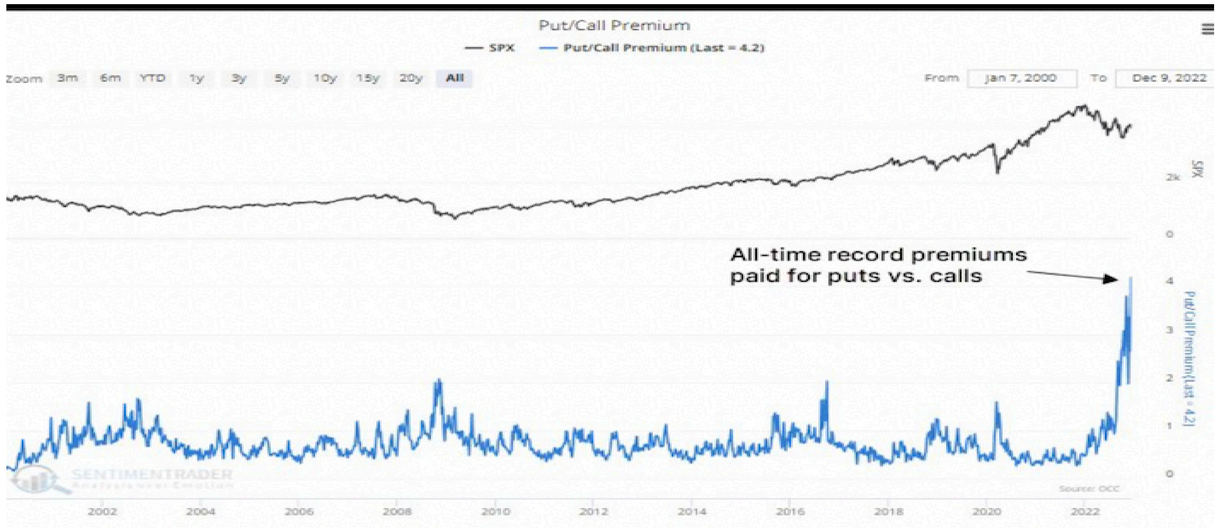
Over the half of excess savings is by top earners

It is capitulation or not?!

- Many market participants are arguing that equity markets have not seen the capitulation yet, because there is not a major outflow of US household equity.
- We believe it is a wrong argument, because, as recently explained, from January 2022 U.S. citizens have higher taxes on gains and therefore we believe that people were not selling positions, but rather buying put options.
- Therefore, analyzing the volume, but especially the premium, of put options (according to several technical analysis, but we include only the chart of Mr. Ansidei), we are at **highest level in the last 22 years! WE CALL IT CAPITULATION!**
- There is even a more shocking fact on statistics. According to the post of Mr. Jain, the volume of option contracts which expire within 24 hours is at highest levels (40% of listed S&P 500 index options volume vs 20% in year 2021!). Mr. Jain explains the phenomenon, as **investors lack of real conviction, underweighted equity, but with fears to miss out a rebound.**



Source: BofA via Mr. Pieper

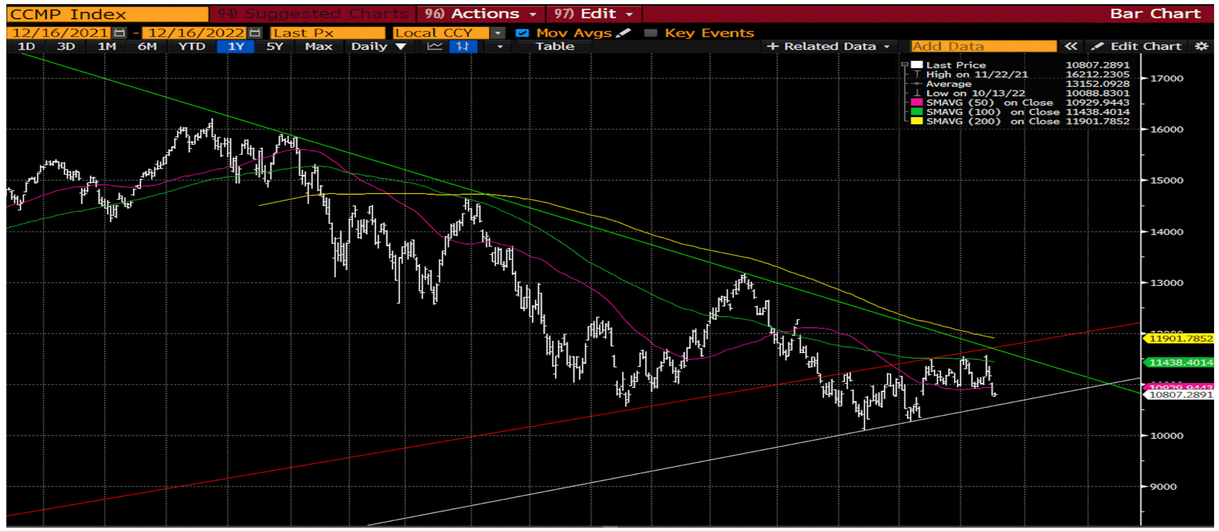


Source: Ansidei + volume of option expiring 24hours double from 2021

Technical analysis

- The substantial correction on the 15th December damaged the uptrend and both indexes, S&P 500 / Nasdaq 100, could not break out the 200d moving average, in the contrary, started to correct.
- For the moment, it is still not a major damage and the indexes are consolidating on the uptrend channel.
- There are not major events on the short term, but tax selling should be finished, meanwhile we expect, share buyback programs are on going and during the first half of January, market should experience inflows from pension funds and according to Mr. Larsen, also liquidity from US debt ceiling.

S&P 500 Index



Nasdaq 100 Index

What we should expect in 2023 - lower inflation

- We would like to summarize the previous slides as follow:
  - **ON INFLATION**
  - The price of **oil and gas had fallen around 40% from their previous highs** and should ease inflation's pressure.
  - For **goods, cars, transport we are in a deflationary environment.**
  - Prices in service is still too robust, but we are normalizing.
  - The **BLS is changing CPI's calculation to further depress inflation**
  - **ON THE FED**
  - Lower inflation means that the FED should change monetary policy. In addition, labor market is weakening. Finally, it is positive, that the FED keeps rates for longer, but is not going higher than 5%
  - **ON GLOBAL MACRO**
  - Lower interest rate hikes means lower USD, which is going to help Emerging markets, European currencies and the JPY. This means also higher USD flows into non-US equities, especially Emerging markets.
  - CEOs extreme depressed sentiment should improve and companies start investing.
  - Having the **Chinese exports falling at steepest pace in more than 2 years,** in addition to internal unrest due to strict Covid measures, it is not a coincidence that Chinese authorities are finally abandoning the tyrannical and arguably pointless lockdowns (how the manager of our best-in-class fund Aubrey argues). This should support the global economy and support the theory of Mr. Yardeni, who is asserting, the economy going to be more resilient than investors think.

What we should expect in 2023 - investment conclusion

- The manager of Aubrey also argues, that Chinese rhetoric towards the West has become marginally less aggressive following the Biden/Xi meeting in November and it is better that there continues to be high level communication between Beijing and Washington rather than none at all.
- Finally, the NATO alliance seems to be holding together, for now at least on the Ukraine's conflict. But of course, the **cost has been terrible** and we start to read since some time now, that USA is not willing to keep such high spending. In addition, there seems to be a global consensus that the use of nuclear weapons is a very bad idea indeed, including, importantly, in China.
- **Conclusion:**

There are several positive triggers for 2023 and having most of experts expecting a recession and double dip of equity markets, we tend to believe, the year 2023 is going to be much more positive, than the majority of the investment community believes.

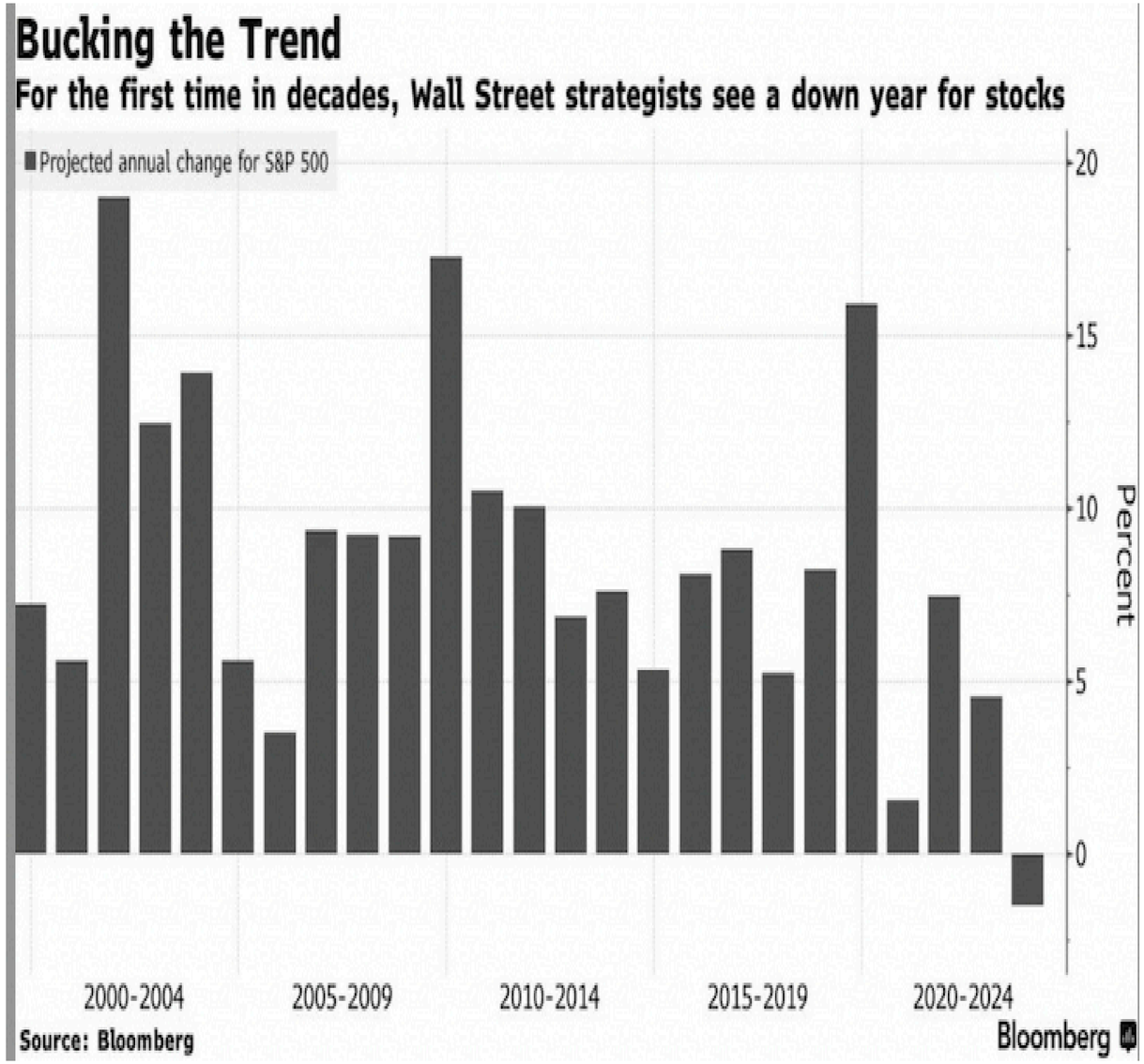
- The **key question is during Q1-Q2**, if the economy going to fall into a deep recession, as many market participants are arguing and for this reason, we will be cautious after the second half of January and have some liquidity, in case equity markets are effectively experience a double dips, which is not the base scenario of KTS.
- But as always explained, we are keeping our core portfolio, which is based on mega trends and uncorrelated strategies.
- We believe that **bonds are going to profit in any scenario in 2023,** because central banks are going to reduce rates in any case, recession or not.

How to catch the upside, but cut the downside

- Having higher interest rates on USD bonds, especially on the short maturities, KTS was working over 3 months optimizing a possible capital protected structure.
- We could finalize the best optimization and we bought in our flagship FoF Optima dynamic a capital protected structure, with a **100% capital protection, in USD**, on the main equity indexes.
- The structure has only 2 years maturity in order to increase the correlation and at a **participation of 107%.**
- It was possible to have such attractive conditions, only by having **Credit Suisse** as issuer. This is because currently the Swiss bank has to pay the highest spreads in order to reach capital markets.
- As recently analyzed in our weekly reports, we do not believe that Credit Suisse will default, on the contrary, the bank has again enough equity capital in order to cover recent scandals and losses and is massively restructuring, which is already good enough for a bondholder.
- We are also convinced, that Switzerland as a country needs 2 major commercial banks, because Swiss mid & small caps need a diversification.
- Therefore, we believe that with such structure, we can profit from any equity market scenario going forward, also in case of a recession, where the FED will have to reduce rates and therefore bond yields will fall, consequently our bond value will increase.
- We are also going to profit, when Credit Suisse spreads are going to stabilize in the next 2 years, which is also our high conviction.

Wall Street analysts are negative for 2023, first time in 2 decades

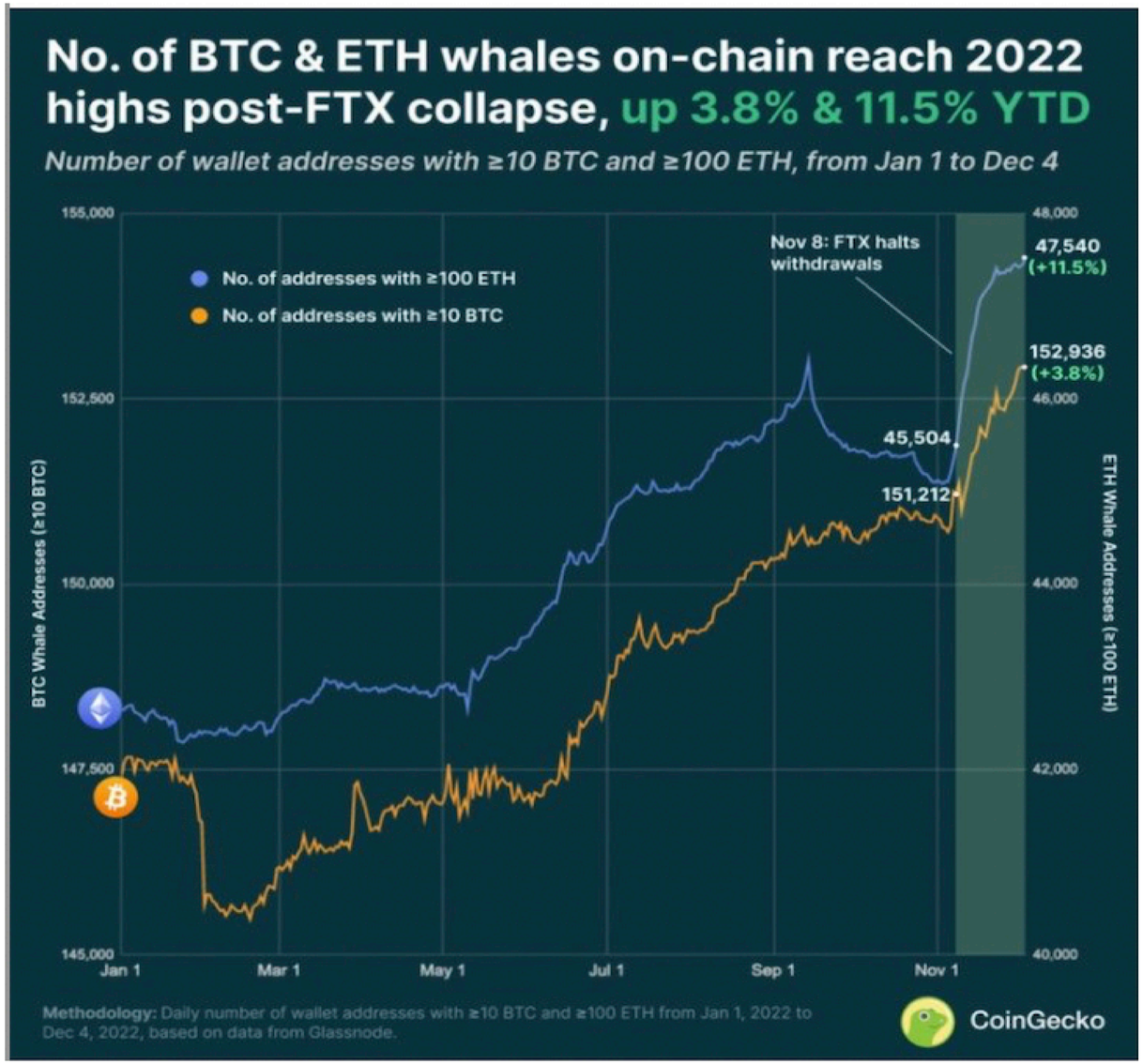
- To complete our previous conclusion on the possible development for 2023, we add this chart, where we can notice that for the **first time in 2 decades, Wall Street strategists see a negative year for stocks ahead.**
- It is well known, that strategists in general, where always predicting positive returns from 5% to 15%, on average 10%.
- Being the first time, where analysts are negative on the year ahead, and listening to most of outlooks, where the investment community is still conservatively invested, it is for KTS a clear bullish contrarian signal.
- We would almost assert, the day, that the investment community has to shift from negative/neutral to positive again on equities, we have to be sure, we are already fully invested.
- This means for KTS, slowly but surely, **it makes sense, to take the risk and anticipate such possible move from the investment community.**



Source: Bloomberg via Mr. Marotz

Big “whale” accumulating Bitcoin and Ethereum

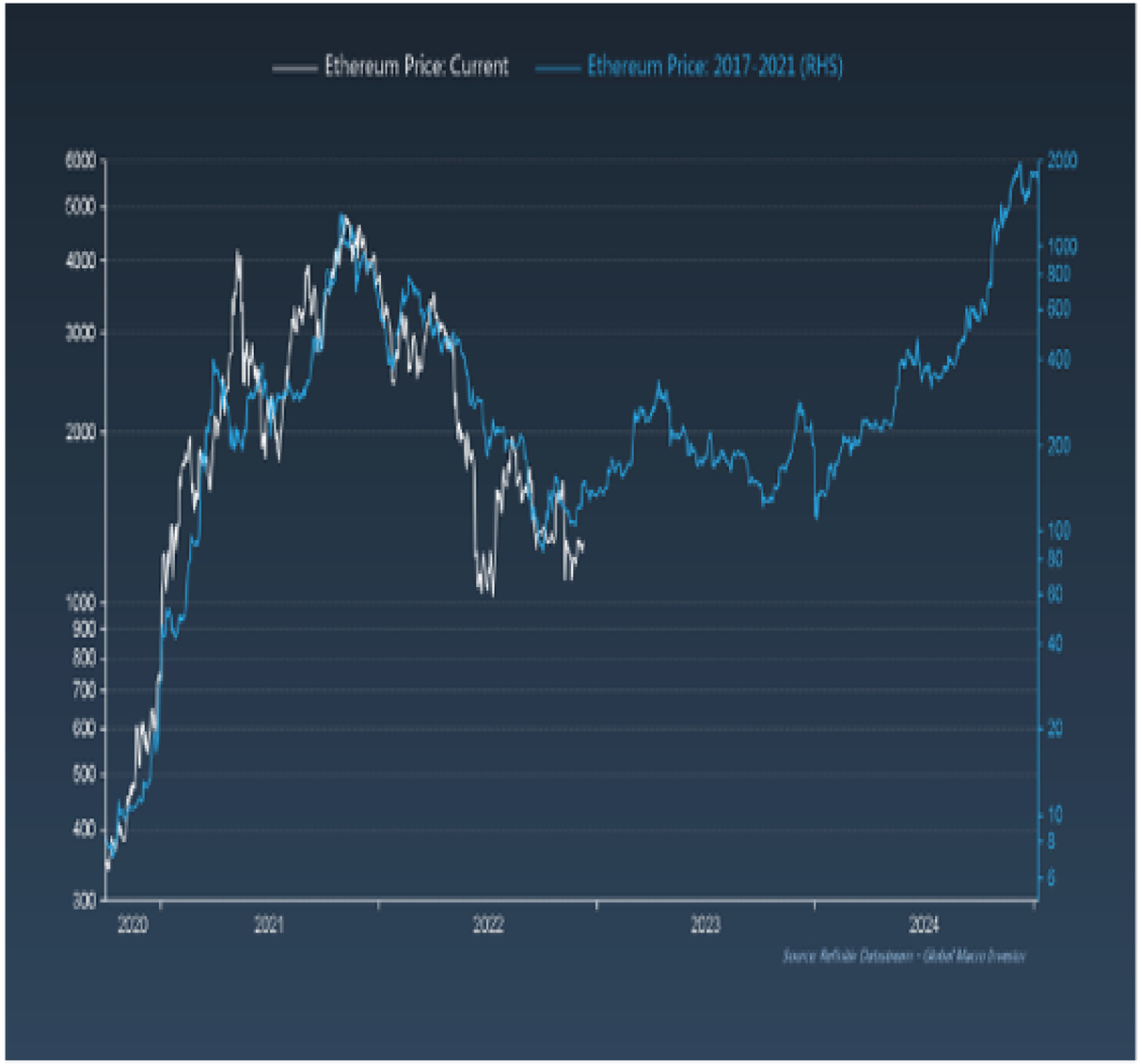
- We are posting the right-hand chart, showing that the number of Bitcoin and Ethereum addresses reached an all-year high in December.
- **Which means, after the FTX’s collapse, big whales are retreating into self-custody and buying the dip.**
- Having “whales” accumulating, this is going to stabilize the price of Bitcoin.



Source: Ms. Monchau-Richard via CoinGecko

Ethereum today vs 2017-2021 analog

- Mr. Pal posted in his latest blog the right-hand chart, showing the analogy of the Ethereum price today with 2017 to 2021.
- KTS was also analyzing again the period 2019 and 2020, because the price of bitcoin started to stabilized in August 2019 anticipating the halving in May 2020.
- Having the next halving in March 2024, KTS would expect crypto currencies to rally again mid 2023 and analyzing the chart of Mr. Pal, it is quite in line with KTS's expectations.
- Therefore, it is time to take into consideration if we would like to invest again long crypto currencies.
- KTS is still analyzing which options are the best.
- We are also reading that the CEO of **Blackrock, Mr. Larry Fink, says that the next generation for markets, the next generation for securities, will be tokenization of securities**. This is quite a strong assertion, which confirms, that crypto is not dead and we are still at the beginning of the cycle, because to have tokenization at a mass level, the path is still long.



Source: GMI top 5 charts of Mr. Pal

General news

- Meanwhile the European Union countries have agreed to set a new limit (EUR 10k) on cash purchases in order to ensure stronger control of cryptocurrency transactions in the region, but not only and also in many other countries are set new lower limit on cash transactions (India, Nigeria, USA 600 USD, etc.), the Pentagon admits, it can't account for over USD 2 Trillion and it is not the fist time.
- **Nuclear fusion** is a reality! Scientists at the National Ignition Facility at the Lawrence Livermore National Laboratory in California announced that they have managed to produce a fusion reaction that produced more energy than it consumed. As we know, nuclear fusion holds the potential to be a practically waster-free and unlimited source of clean energy. The negative side of the news is, the path to have nuclear fusion connected to the electricity grid is still very long and as you know, climate scientists have warned, that the world does not have decades to wait until the technology is potentially viable to zero out greenhouse gas emissions.

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