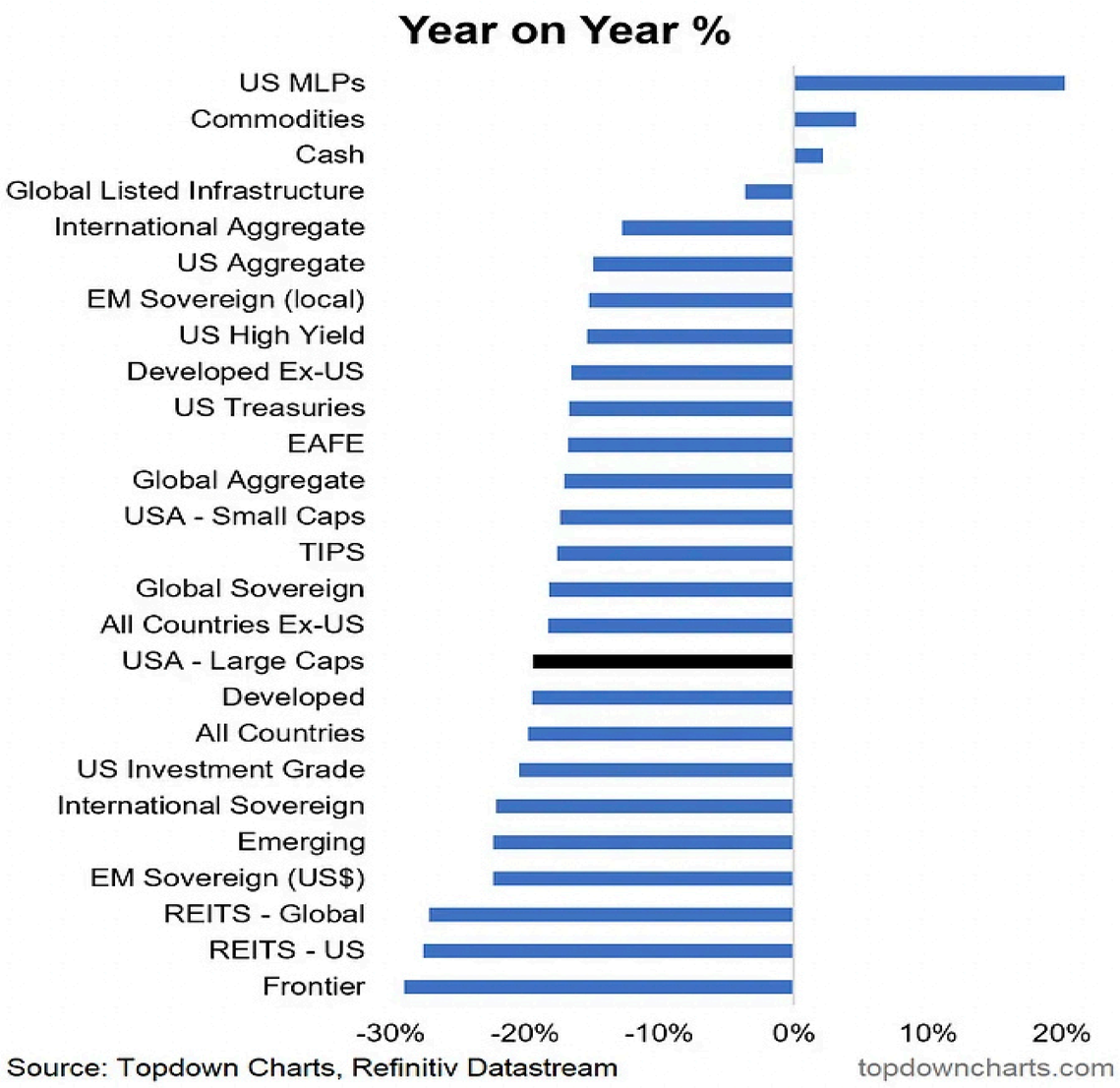
KTS
CAPITAL
MANAGEMENT

KTS weekly update Nr. 1

The 6th of January2023

2022 performances: no where to hide

- The **S&P 500 Index** closed at **-19.41 %** (total return including dividends **-18.13%)**
- In the contrary the **DOW Index was only -8.8%** (-6.86% total return), due to the energy sector reaching +64% (tot return)
- The **Nasdaq Index -33.10%** (-32.51% tot ret)
- The **MSCI World -19.46%** (-17.71% tot ret)
- The **20+ Treasury -31.24%** total return
- **Emerging market debt -22.44%** (-18.64% tot return)
- **US High yields -15.88% , but "only" -11% total return.** The energy sector is an important contributor.
- **Gold was flat in USD and CHF, but +11% in GBP and +5.5% in EUR**
- The **oil price ended the year with around +4%** , but was +69% on the highs in March 2022 after the Ukraine-Russia conflict and with market participants speculating prices over 150 USD! We are 40% lower from such highs, fortunately.
- **Bitcoin and Ethereum -66% , Solana and alt coins -90%**



2022: the worst multi-asset year since 1937: it can be only better?

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

Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40	Year	S&P	10-Yr	60/40
1928	43.8%	0.8%	26.6%	1947	5.2%	0.9%	3.5%	1966	-10.0%	2.9%	-4.8%	1985	31.2%	25.7%	29.0%	2004	10.9%	4.5%	8.3%
1929	-8.3%	4.2%	-3.3%	1948	5.7%	2.0%	4.2%	1967	23.8%	-1.6%	13.6%	1986	18.5%	24.3%	20.8%	2005	4.9%	2.9%	4.1%
1930	-25.1%	4.5%	-13.3%	1949	18.3%	4.7%	12.8%	1968	10.8%	3.3%	7.8%	1987	5.8%	-5.0%	1.5%	2006	15.8%	2.0%	10.3%
1931	-43.8%	-2.6%	-27.3%	1950	30.8%	0.4%	18.7%	1969	-8.2%	-5.0%	-7.0%	1988	16.6%	8.2%	13.3%	2007	5.5%	10.2%	7.4%
1932	-8.6%	8.8%	-1.7%	1951	23.7%	-0.3%	14.1%	1970	3.6%	16.8%	8.8%	1989	31.7%	17.7%	26.1%	2008	-37.0%	20.1%	-14.2%
1933	50.0%	1.9%	30.7%	1952	18.2%	2.3%	11.8%	1971	14.2%	9.8%	12.4%	1990	-3.1%	6.2%	0.6%	2009	26.5%	-11.1%	11.4%
1934	-1.2%	8.0%	2.5%	1953	-1.2%	4.1%	0.9%	1972	18.8%	2.8%	12.4%	1991	30.5%	15.0%	24.3%	2010	15.1%	8.5%	12.4%
1935	46.7%	4.5%	29.8%	1954	52.6%	3.3%	32.9%	1973	-14.3%	3.7%	-7.1%	1992	7.6%	9.4%	8.3%	2011	2.1%	16.0%	7.7%
1936	31.9%	5.0%	21.2%	1955	32.6%	-1.3%	19.0%	1974	-25.9%	2.0%	-14.7%	1993	10.1%	14.2%	11.7%	2012	16.0%	3.0%	10.8%
1937	-35.3%	1.4%	-20.7%	1956	7.4%	-2.3%	3.6%	1975	37.0%	3.6%	23.6%	1994	1.3%	-8.0%	-2.4%	2013	32.4%	-9.1%	15.8%
1938	29.3%	4.2%	19.3%	1957	-10.5%	6.8%	-3.6%	1976	23.8%	16.0%	20.7%	1995	37.6%	23.5%	31.9%	2014	13.7%	10.7%	12.5%
1939	-1.1%	4.4%	1.1%	1958	43.7%	-2.1%	25.4%	1977	-7.0%	1.3%	-3.7%	1996	23.0%	1.4%	14.3%	2015	1.4%	1.3%	1.3%
1940	-10.7%	5.4%	-4.2%	1959	12.1%	-2.6%	6.2%	1978	6.5%	-0.8%	3.6%	1997	33.4%	9.9%	24.0%	2016	12.0%	0.7%	7.5%
1941	-12.8%	-2.0%	-8.5%	1960	0.3%	11.6%	4.9%	1979	18.5%	0.7%	11.4%	1998	28.6%	14.9%	23.1%	2017	21.8%	2.8%	14.2%
1942	19.2%	2.3%	12.4%	1961	26.6%	2.1%	16.8%	1980	31.7%	-3.0%	17.8%	1999	21.0%	-8.3%	9.3%	2018	-4.4%	0.0%	-2.6%
1943	25.1%	2.5%	16.0%	1962	-8.8%	5.7%	-3.0%	1981	-4.7%	8.2%	0.5%	2000	-9.1%	16.7%	1.2%	2019	31.5%	9.6%	22.7%
1944	19.0%	2.6%	12.4%	1963	22.6%	1.7%	14.2%	1982	20.4%	32.8%	25.4%	2001	-11.9%	5.6%	-4.9%	2020	18.4%	11.3%	15.6%
1945	35.8%	3.8%	23.0%	1964	16.4%	3.7%	11.3%	1983	22.3%	3.2%	14.7%	2002	-22.1%	15.1%	-7.2%	2021	28.7%	-4.4%	15.5%
1946	-8.4%	3.1%	-3.8%	1965	12.4%	0.7%	7.7%	1984	6.1%	13.7%	9.2%	2003	28.7%	0.4%	17.4%	2022	-18.1%	-16.5%	-17.5%

1931, 1941, 1969 and 2018 all asset classes were negative, BUT only in 2022 both the S&P 500 Index and the 10-year Treasuries were down more than 10%

Analysis of the KTS' asset allocation for 2022

Positive contributors?

1. **Fixed Income:** positive contributor, meanwhile traditional bonds experienced a dramatic correction.
2. **Energy:** our overweight paid off and the long/short green strategy was basically flat vs the "green etf" PBW US with a -46.33% for the year 2022.
3. **Gold:** Flat in USD and CHF, but positive in GBP, EUR. Nevertheless, gold miner's performance very disappointing.
4. **Optima Dynamic fund:** ended the year negative, but clearly outperformed peers. The diversification of strategies instead of asset classes once again worked well, though, can still be improved.
5. Tremendous positive performance of our private equity investment into the green and sustainable Croatian company **Rimac automobili,** meanwhile comparative companies basically all collapsed during 2022 (Rivian, Lucid, etc.). Many of our clients could actually reach a positive performance for 2022 due to such significant "booster".
6. **M&A strategy:** light negative performance, but could limit the drawdown. Nevertheless, we are going to sell the strategy in order to invest in more dynamic investments, having currently long-term attractive investment opportunities and being KTS convinced, over the mid term, equity markets are going to increase from this levels.
7. **Put options** marginally helped to limit the drawdown, but we expected a better optimization. It was a tough year for options.

Analysis of the KTS' asset allocation for 2022

Positive contributors?

8. Trading the QQQ US from the lows of June 2022, especially selling by opening gaps was a value added vs a simple buy & hold strategy and disappointing L/S strategies. Going forward, being difficult to trade put options, it will be of vital importance to combine such trading with the technical analysis, especially at current critical support levels combined with still very weak fundamentals. In case of a break down of the 200d moving average, we can optimize our equity exposure, by totally selling the QQQ position and simultaneously going short, allowing us to reduce our net equity exposure from around 2/3 to 1/3 . The idea would be to further optimize, by buying some put options for only a 1/4 of the equity long portfolio, if the levels of volatility are not too prohibitive. We are analyzing the maturity March 2023 and it would costs around 0.27% of the portfolio, which is an acceptable costs, especially taking into consideration, that it is still general consensus, during H1 2023 equity markets will need to correct further.

9. Our **uncorrelated strategies** helped to stabilize our already balanced portfolio. In fact, the Swisscom and Fasanara VC strategies were flat, and the crypto arbitrage slightly positive.

Analysis of the KTS' asset allocation for 2022

What went wrong?

1. We should have had rebalanced our Investment into **Vietnam,** which was performing extremely well up to June 2022, meanwhile global equity markets were already into bear market territories.
2. We should have had increased our stop loss for **gold miners,** which were over +30% in February 2022. Even if we have to be honest, it was a very tough call, because gold was at major long-term breakout levels combined with extreme geopolitical tensions and therefore it would not make sense, to sell positions in such environment and with such strong technicals.
3. The **Biotech basket** was over +20% in June 2022 due to an acquisition of one position in the portfolio (Turning Point Therapeutics), but ended the year negative, having re-invested the profit.
4. We have to improve our **hedge on the USD** and the bank costs for smaller portfolios**.** In order to optimize the USD risk in the future, we are reducing our USD exposure by selling some investments as for example the M&A strategy or fixed income strategies, which are reaching 5% to 7% yields p.a. but the increasing hedging costs in USD are basically wiping off such yields.
5. KTS expected a more resilient **Emerging market debt.** In the correction we added positions, believing the asset class is very attractive and can reach above average returns in the years ahead. On the equity side, our best-in-class fund Aubrey emerging market lost part of the past outperformance and our Vietnam's investment, which was very steady during H1 2022 also collapsed in the second half of the year, in line with equity markets. We were not dynamic enough and we are going to optimize our re-balancing strategy in the future. We also added a new position in the space, the new best-in-class emerging market fund Flossbach emerging market, which has proven to have a solid track record.

Analysis of the KTS' asset allocation for 2022

What went wrong?

6. KTS sold disappointing strategies like the Long/short funds Alkeon, Fundana or 2xIdea.

7. The biggest disappointment for the year 2022 are our funds based on the **Volatility "booster"** , which were not helping to limit the drawdown, in the contrary any long volatility attempt costed performance. As explained in our market outlook 2023, the year 2022 was a year of the known unknown and therefore, the volatility index did not spike, like for example during the pandemic year 2020. We reduced our exposure in such strategy, having newly bought the capital protected structure on the main equity indices, as recently explained in our weekly report nr. 50 on the 16th December 2022.

8. Our strategy of **selling volatility** disappointed, mainly because our counter party did not allow to keep liquidity on the account, being interest rates in CHF still negative. This fact recently changed and we are confident, that the timing on holding liquidity and being allow to wait for the right investment opportunities, will help KTS to optimize the strategy's result.

9. Our best-in-fund value fund Classic global was not limiting the drawdown as per manager's simulation last year, in case interest rates would increase.

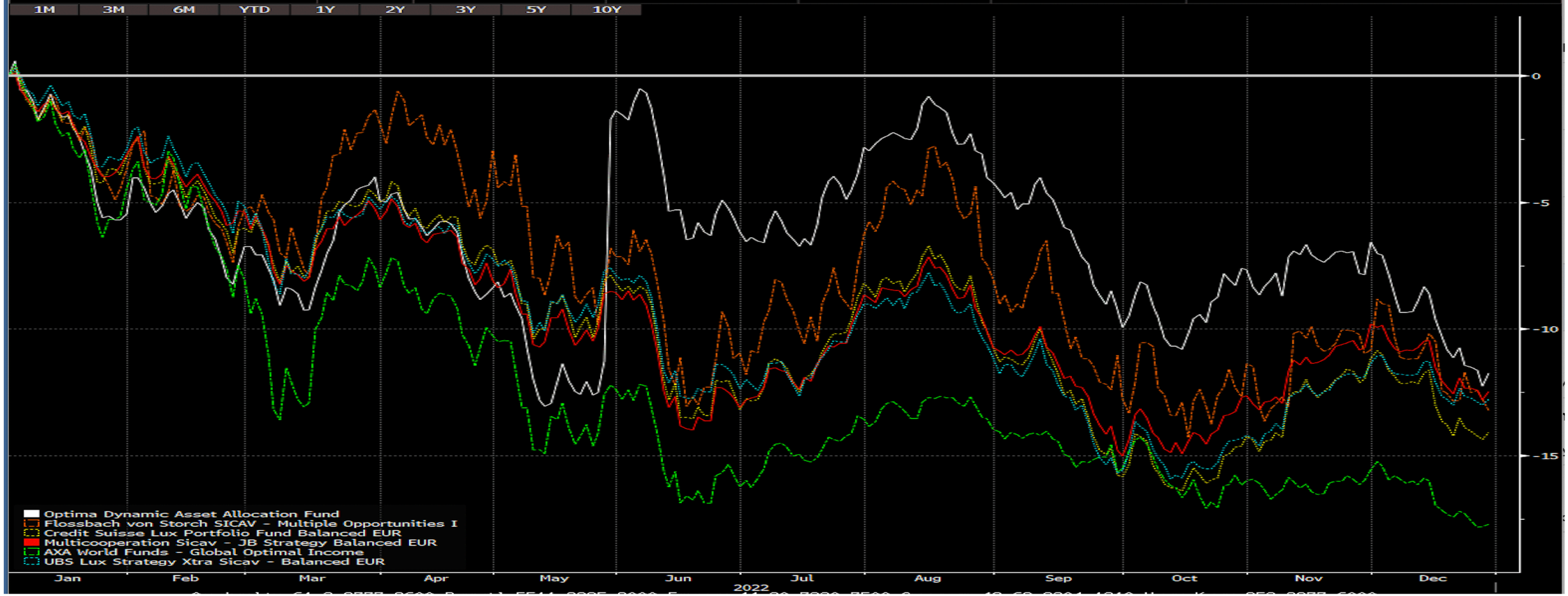
10. Also the best-in-class Alpora innovation and Tramondo were not performing as expected, but we still keep the funds for the time being.

The flagship balanced fund Optima dynamic beats again top peers

OPTIMAE LE Equity | Settings | Comparative Returns

Range 01/03/2022 - 12/29/2022 Period Daily No. of Period 360 Day(s) Table

	Security	Currency	Price Change	Total Return	Difference	Annual Eq
1)	OPTIMAE LE Equity	EUR	-11.74%	-11.74%	1.47%	-11.89%
2)	FVSTMOR LX Equity	EUR	-13.72%	-13.21%	--	-13.38%
3)	CSPLBAL LX Equity	EUR	-14.08%	-14.08%	-.87%	-14.26%
4)	JBPSBEB LX Equity	EUR	-12.47%	-12.47%	.74%	-12.63%
5)	AXAGLOI LX Equity	EUR	-17.73%	-17.73%	-4.51%	-17.95%
6)	UBXBALB LX Equity	EUR	-12.78%	-12.78%	.43%	-12.94%



The Optima dynamic fund (white line) beats also in 2022 our best-in-class per excellence balanced fund Flossbach and all major peers

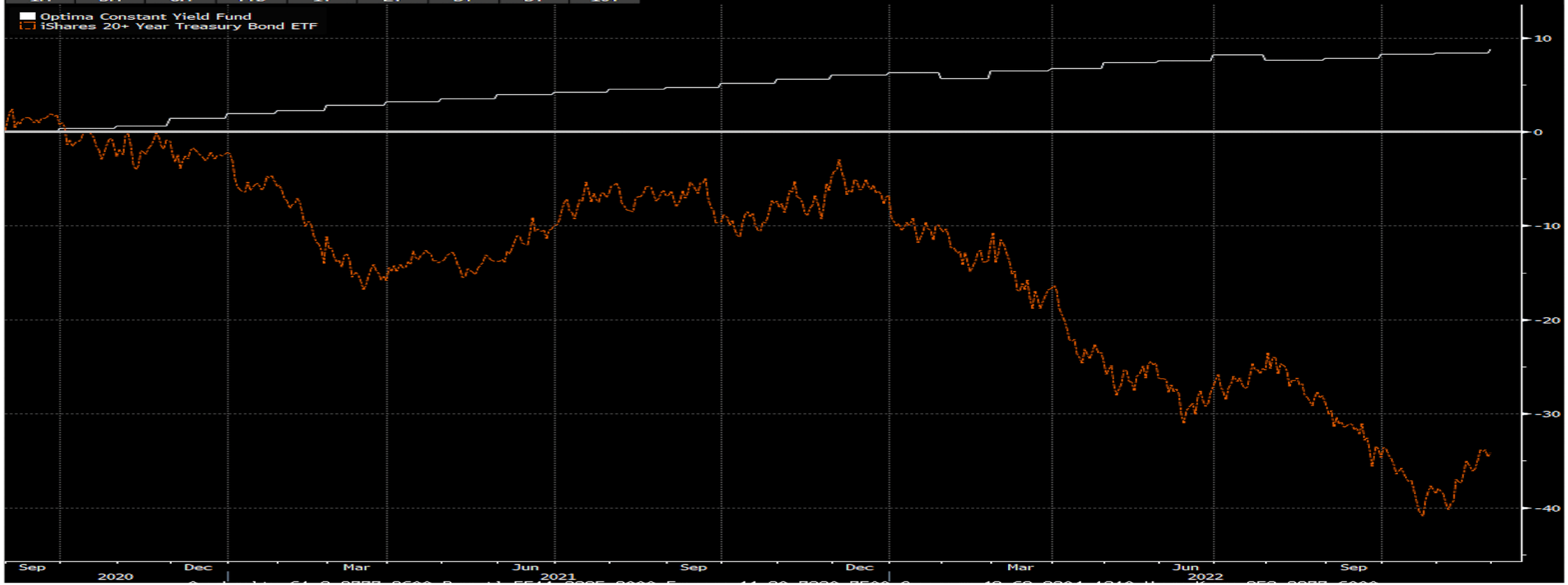
KTS's fixed income strategy's positive result helped to stabilize our portfolios

OCYFUSD LE Equity | Settings | Comparative Returns

Range 08/31/2020 - 11/30/2022 Period Daily No. of Period 821 Day(s) Table

	Security	Currency	Price Change	Total Return	Difference	Annual Eq
1)	OCYFUSD LE Equity	USD	8.77%	8.77%	42.92%	3.81%
2)	TLT US Equity	USD	-36.66%	-34.14%	--	-16.95%
3)						
4)						
5)						
6)						

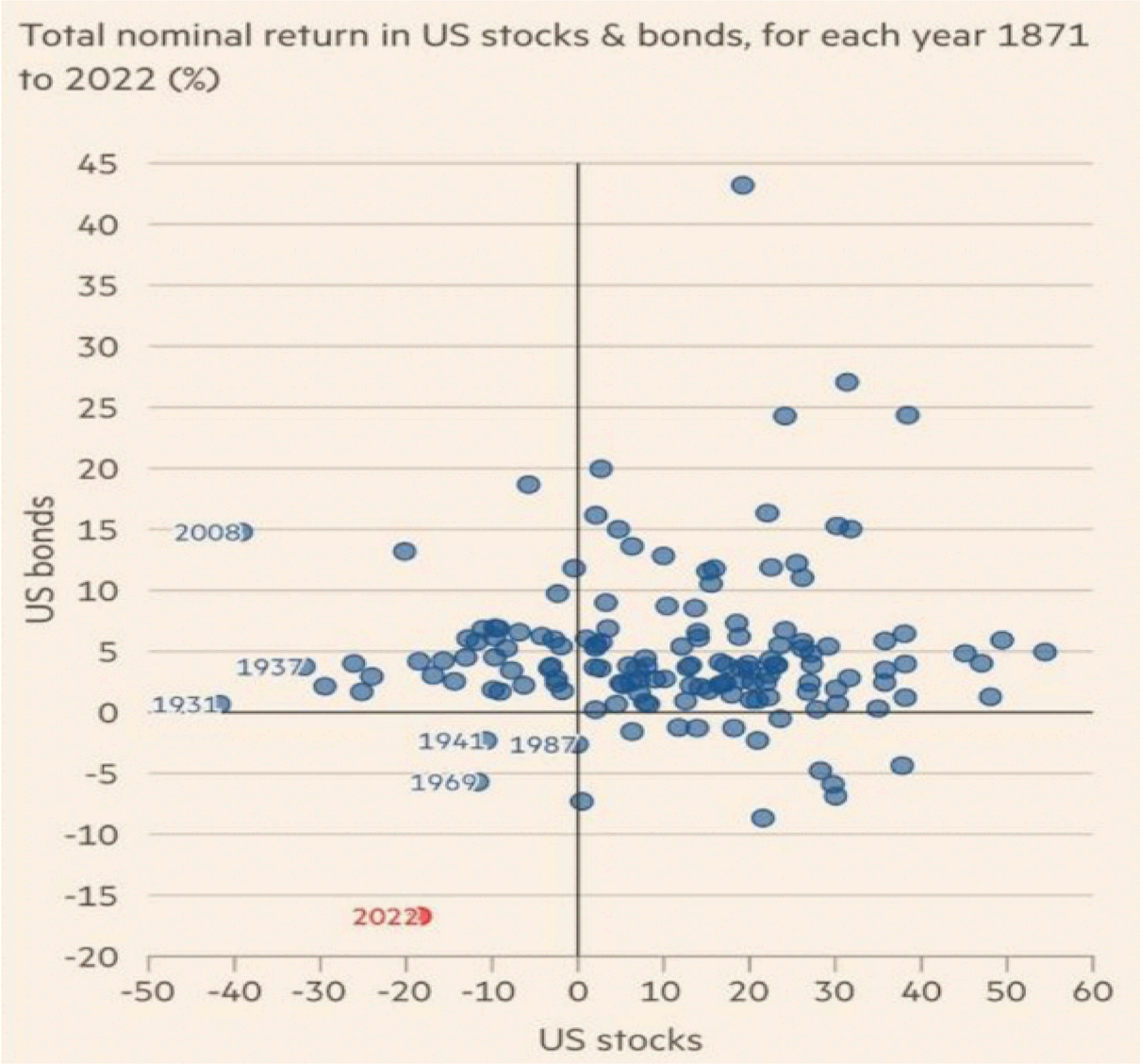
1M 3M 6M YTD 1Y 2Y 3Y 5Y 10Y



The optima constant yield fund positive return helped to stabilize our portfolios, in the contrary to global bonds, which experienced a dramatic correction

2022: the worst year ever for stocks and bonds since 1871

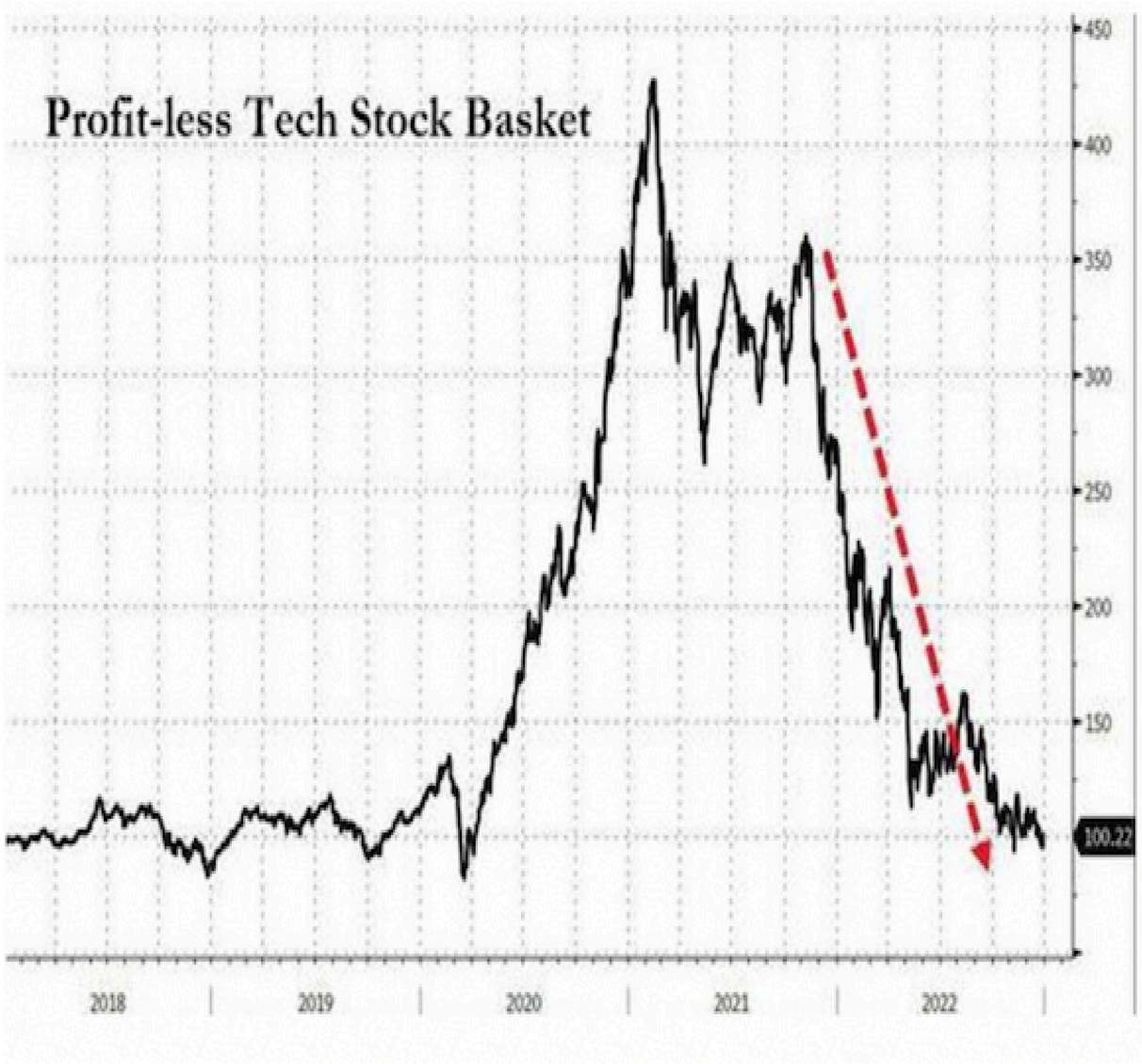
- We would like to include again some final charts of the year 2022 to give an idea of the magnitude of the market's correction, which is in fact the most dramatic in history.
- We start with the historical performance of bonds and equity, were never in history, **both asset classes lost basically on the same magnitude over -20% resulting a financial wealth destruction, even meltdown, over USD 35 to 40 trillion, which is 1/3 of the global GDP.**
- USD 12 trillion US stock market alone of which 5 trillion only the FAANGS, therefore the USD 32 billion of one of the biggest fraud ever, namely the crypto platform FTX is "peanuts" in comparison. Also the total loss wiped off from the total crypto market is quite meaningless.
- We are reading a statement of Mr. Eric Balchunas arguing, that **for 2022 only a diversification out of traditional asset classes would have help mitigate investment losses. This is was exactly KTS is trying to do since 6 years now.**



Source: Financial time

2022: non-profit tech -90%

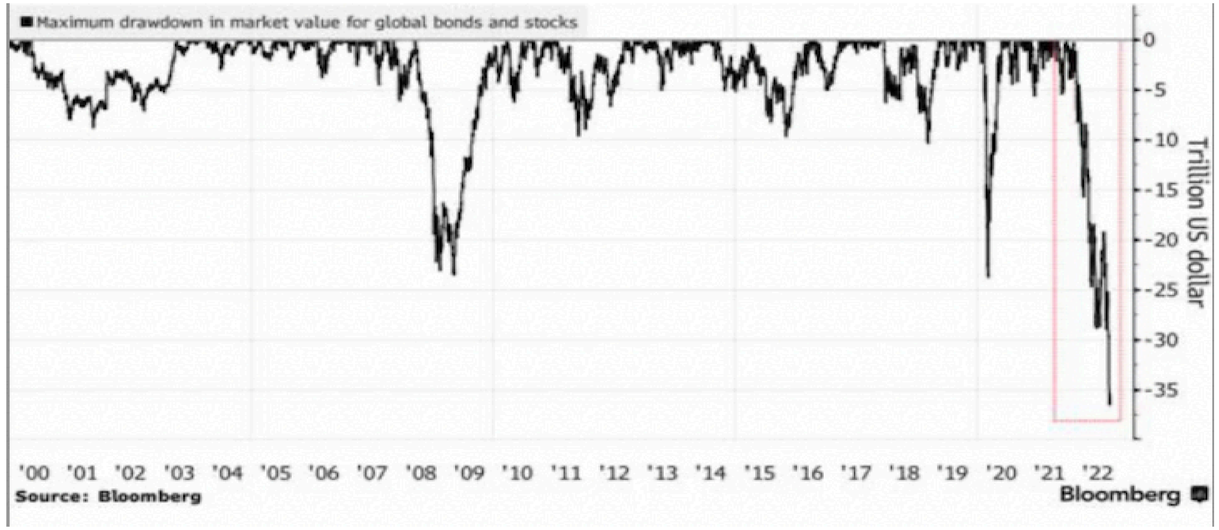
- The following chart is giving the perfect idea of the correction's magnitude in 2022.
- Non-profit tech, or "meme" stocks, as also SPACs, hype IPOs, cryptos, NFTs all corrected 90% in the best case or defaulted.
- Therefore it is right to assert, the correction and the sentiment during 2022 definitely reached the same magnitude of the tech bubble in the year 2000 or GFC 2008.
- For this reason we do not take serious any chart comparison of the Nasdaq Index 2000 vs 2022 and expect a further dramatic correction, because stocks which were not correcting 80% are solid companies, with net cash and massive share buyback programs, which was not the case back in the tech bubble.
- Nevertheless, tech leaders as Netflix, Paypal, Meta an many others corrected almost 80% but still have net cash positions and positive FCF. Over **USD 7 trillion in stock market cap has been erased only from the Nasdaq 100 and in 2008, even if the drop was -41.9%, it was "only" USD 1 trillion.**



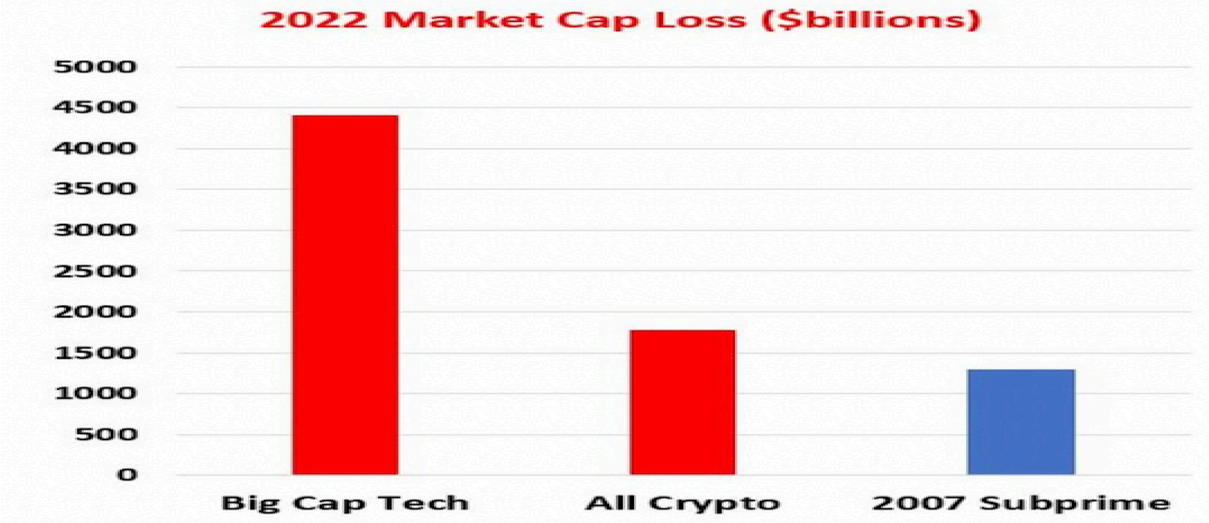
Source: zerohedge via Syz group

2008: was nothing compared to 2022

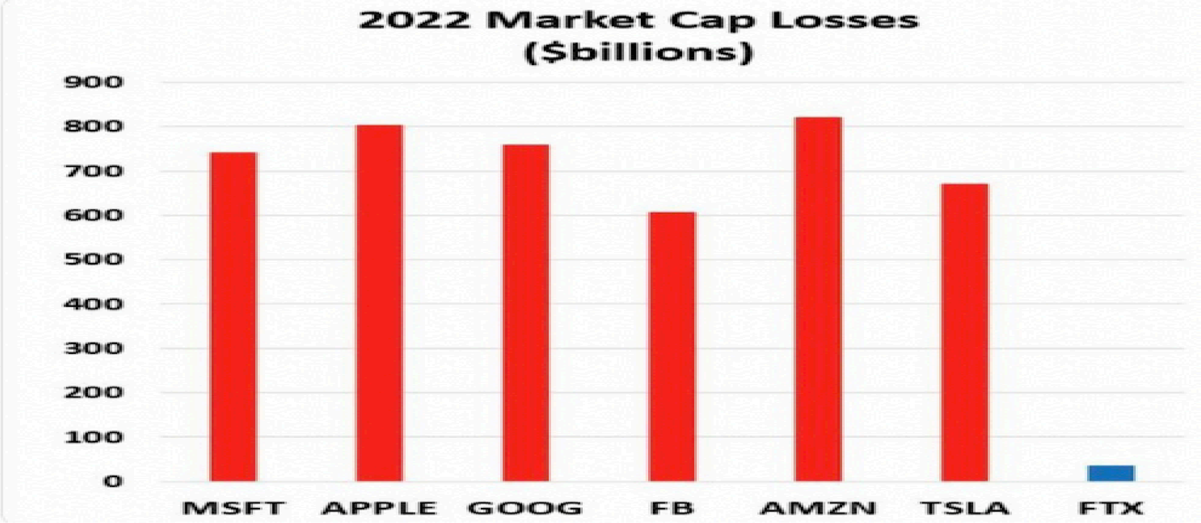
- Over USD 35 trillion in wealth destruction during 2022 is more than the double of the GFC 2008. Those are truly dramatic numbers, of course money also inflated during such period of time.
- The market cap loss during the subprime crisis in 2007 and the total loss of all cryptos are still insignificant vs the total loss of the big tech companies (chart below-left).
- Finally, even if the FTX's debacle is one of the biggest fraud ever, is "peanuts" vs the market cap losses of the big tech.



USD 35 to 40 trillion in wealth destruction (Source Bloomberg)



Subprime and all crypto insignificant losses vs bit tech cap



FTX's debacle insignificant vs market cap losses of the FAANGS

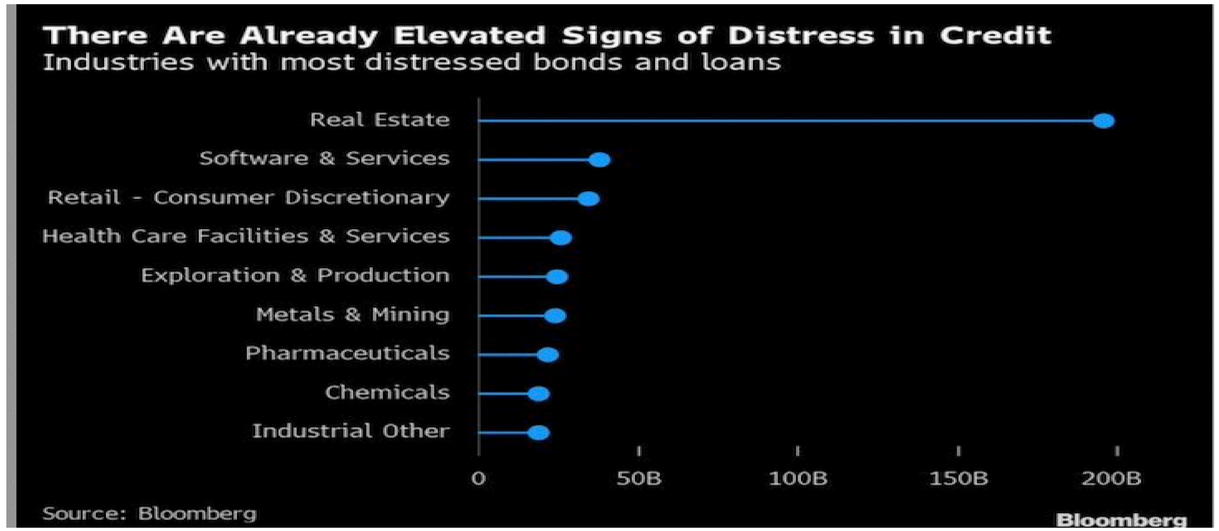
The only winner of 2022: the energy sector

- KTS could profit from the overweight in energy during the year 2022. The sector performed over 60% and is basically the only segment, which closed with a positive performance in 2022.
- Normally after such tremendous outperformance, it would be time for a sector rotation, but as we have recently analyzed, the energy sector still has a very attractive valuation and companies need to increase investments and capex, especially in alternative energies, in order to meet CO2 reduction regulations and improve ESG rating in order to attract investors.
- Cash flows of the energy sector are strong, therefore will be also share buyback programs and dividends. We stay exposed with our experts, which are investing in energy and materials expose to the “green transition” mega trend. But we are going to continue to trade the QQQ US as the most sensitive sector in case equity market would rebound.
- The year 2022 was an “alpha year” having stock selection making the clear outperformance and 2023 going to be the same. KTS is aware and wants to be more dynamic.

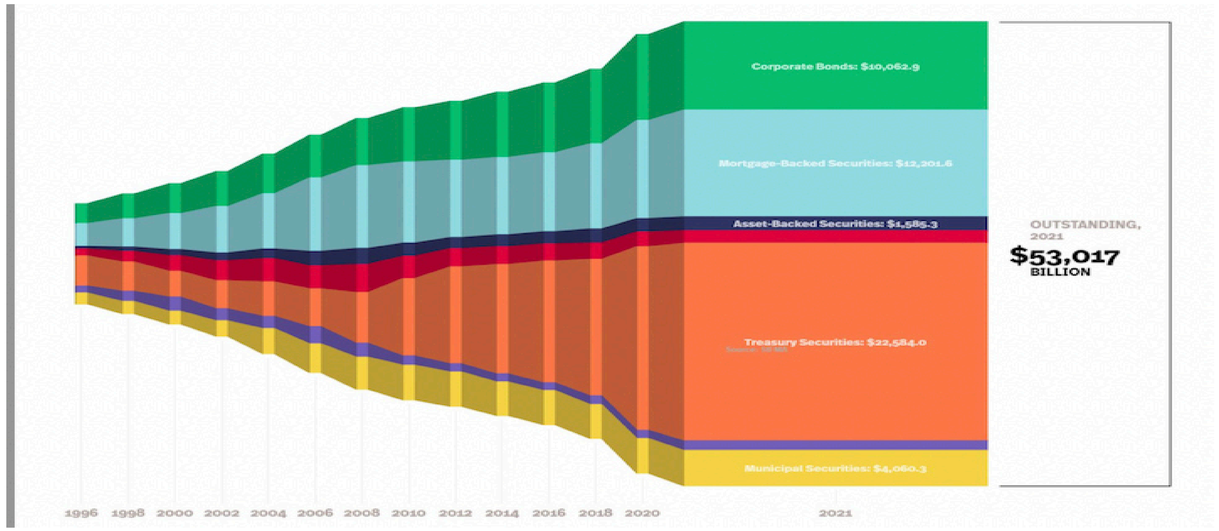
Source: Financial time

First signs of distress in bonds and loans: really?

- Market participants are arguing, there are already serious signs of credit distress, especially on the US real estate sector (see first chart).
- **Around USD 298 bn bonds and loans are in distress.**
- **But the total outstanding debt volume is USD 53’017 bn, therefore we are talking about 0.56%**



Credit distress in real estate (source Bloomberg)

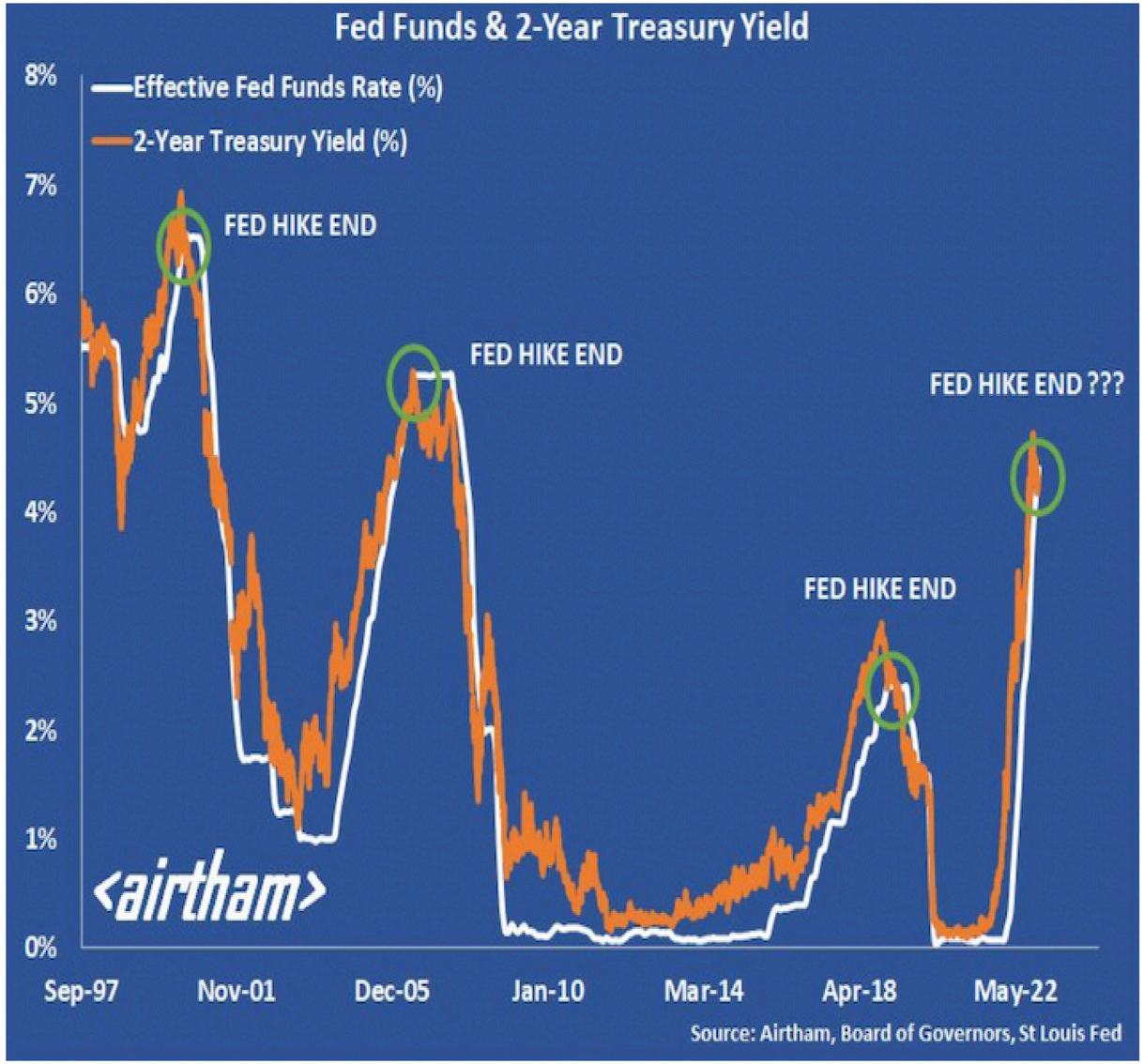


Total outstanding debt: USD 53’017 billion: what is USD 298 bn?

The FED hikes have ended?

- We like the right-hand chart, courtesy Mr. Apte, where we can analyze the historical correlation between the 2-year treasury yield and the FED funds rate.
- As we can notice, the 2-year Treasury yields are a leading indicator of the FED fund rate and historically, during a **hiking cycle, whenever the FED fund rate has exceeded the 2-year yields with declining inflation, the FED has stopped hiking every time.**
- This is the actual scenario, even more, we are starting the year 2023 with 4 obvious fact:

1. The most well-announced recession in history
2. Most market participants are expecting equity market to fall further, at least 10%.
3. The FED is expected to pivot in Q1, only because of equity markets collapsing.
4. The US housing experienced the fastest slowdown in history and can get only worse.



Source: Mr. Apte / Airtham

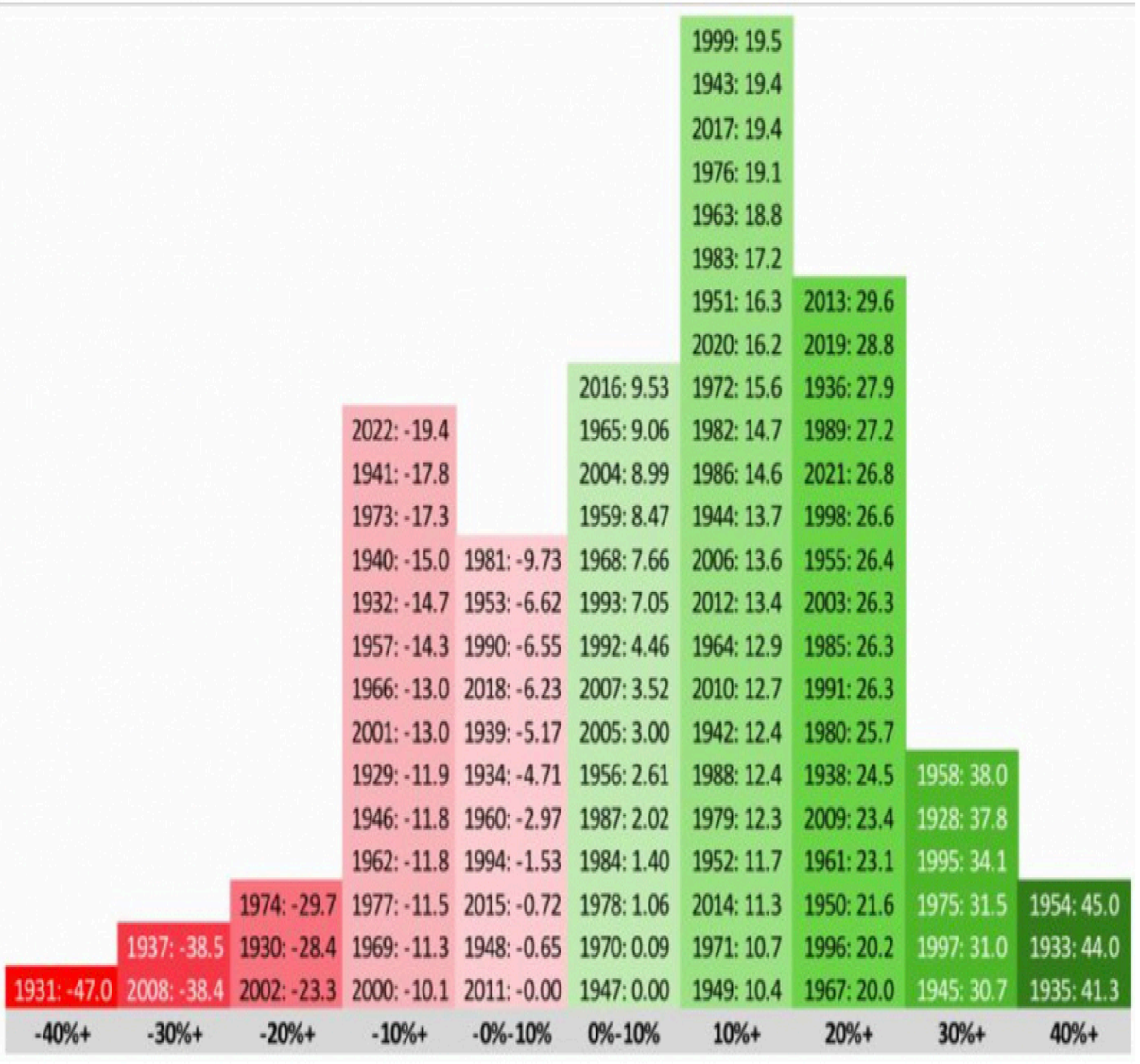
FINRA margin debt still contracting - consolidation still not over?

- Mr. Apte is rightly pointing out, historically a market bottom coincides only with the margin debt expansion.
- **Unfortunately in November 2022 the Finra margin debt showed further contraction and therefore it is still to early to call the bottom of the equity market.**
- We agree with his opinion, that a **stabilization of Finra margin debt helps to differentiate between a bear market rally and an onset of a new bull market.** Investors are going to invest aggressively again, and therefore increase leverage, once they sense, equity markets bottomed.
- Unfortunately we are still consolidating at a crucial support level and with no sign of the FED to pivot, we also can not see short term triggers for a strong rebound of equity markets and therefore we are carefully monitoring the risk of an eventual breakdown of the 200d moving average.

Source: Mr. Apte / Airtham

After an extreme negative 2022, some positive statistic relevances

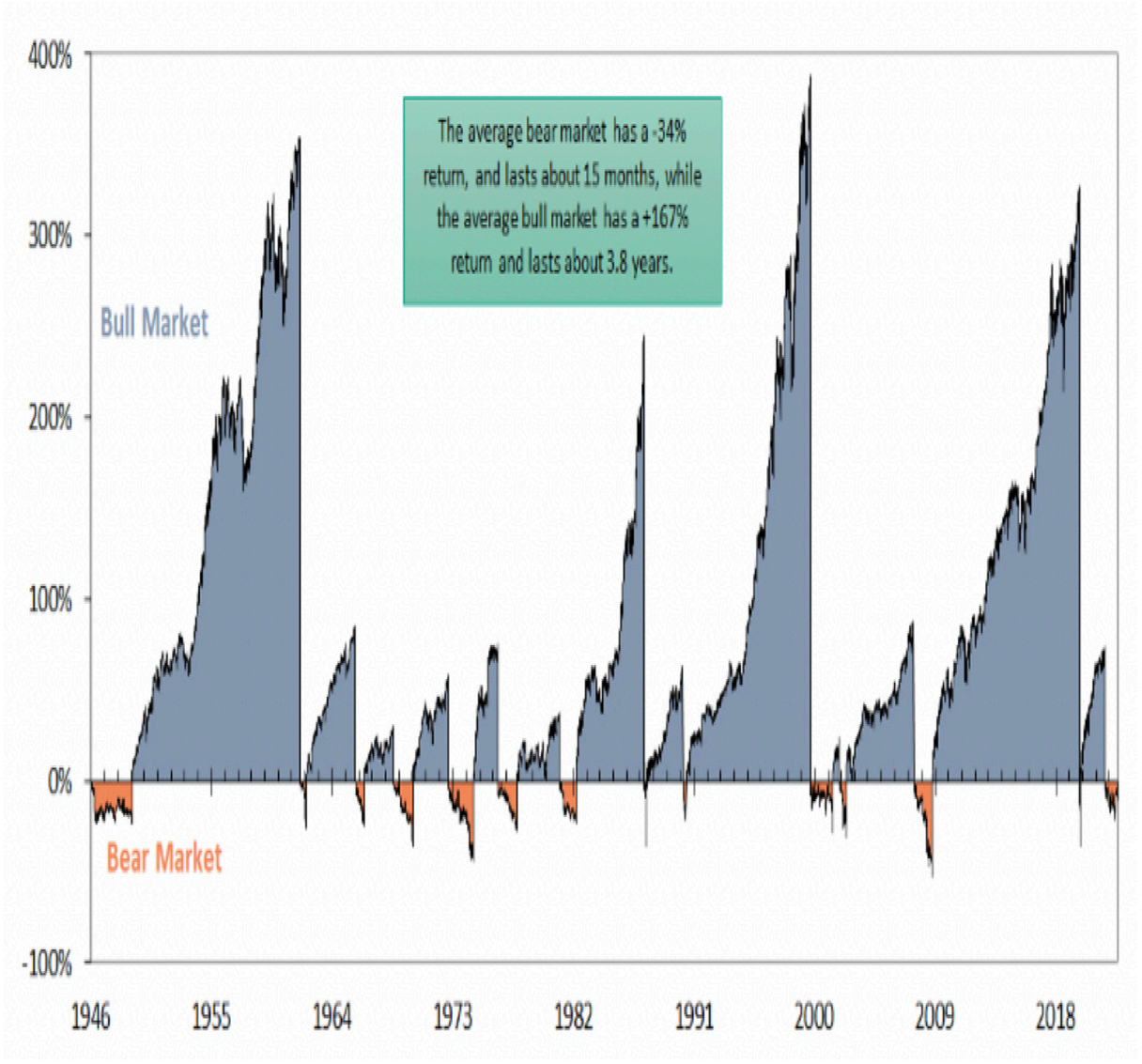
- We include the latest blog of Mr. Budelmann, CIO of Bergos AG, which gives some interesting historical extremes.
- The S&P 500 index closed the year 2022 with a -19.4% and therefore with the largest annual decline since 2008's drop of over 38% .
- But 2022 was historically the fourth highest total of 1%+ daily declines in the last 70 years. Only 2008, 2002 and 1974 were higher. In addition, 2022 had more than half of all months (7) experiencing a decline at least -2.5% and 5 of those had at least -5% .
- Analyzing the right-hand chart, only 2 other years in the S&P 500 Index's history had as many months with a 2.5% decline (1931 and 1937) and another 4 had 6 months with declines of at least 2.5% (1932, 1957, 1974, and 2008).
- The positive note of Mr. Budelmann: of the **6 similar years, the S&P500's median change in the following year was +28%** , except 1932. We do not believe the actual situation is comparable with 1932.



2022: a year of many extremes, can only get better?

Every bear market has ended and has led to a longer bull market

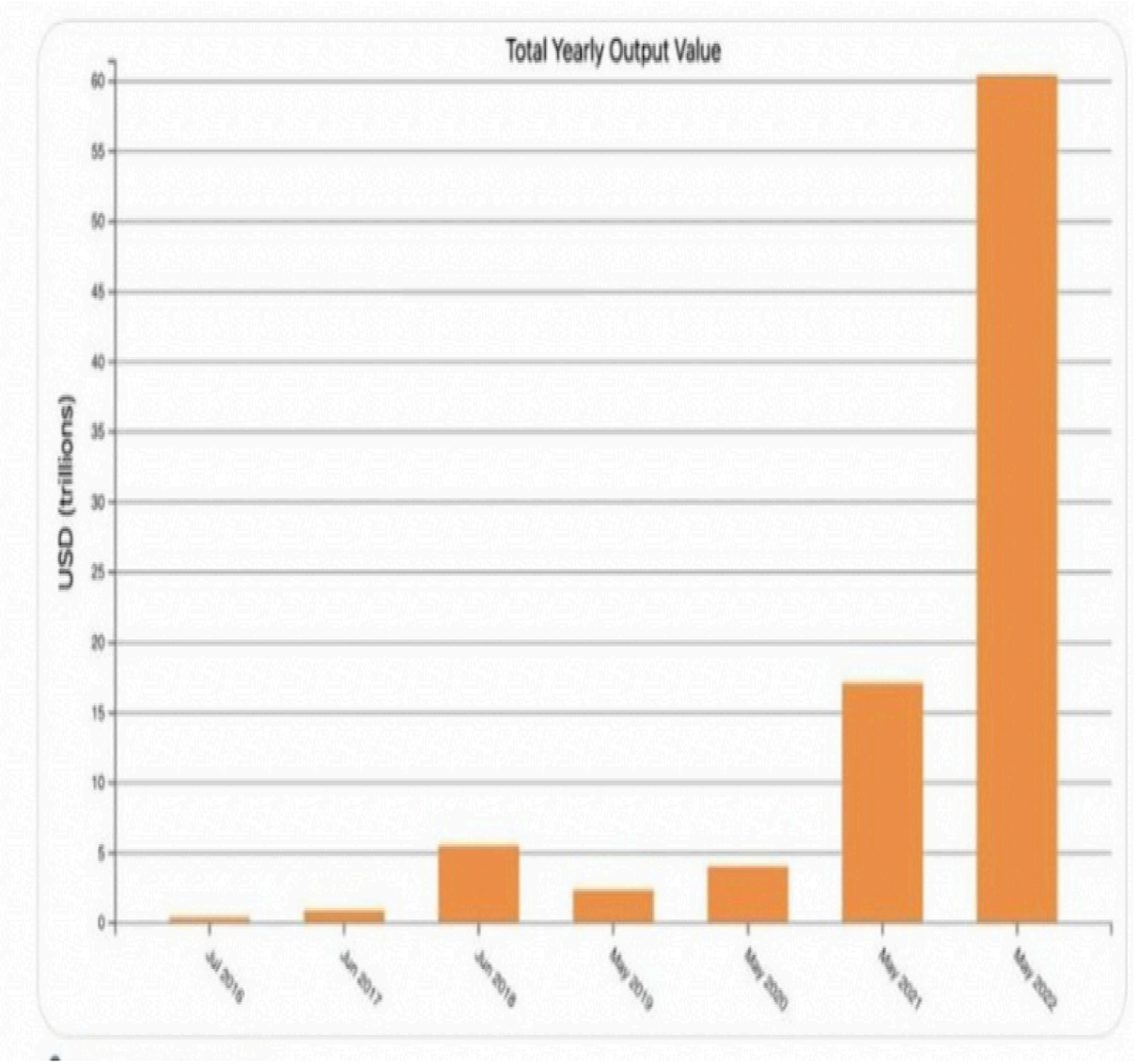
- In oder to enter the new year with some positivity, we would like to post the following chart, courtesy Mr. Edward Jones, whereby we can analyze, that any **bear market in history has one day ended, but most importantly, was followed by a longer and stronger bull market!**
- Reading outlooks of major research houses, we would summarized, that general consensus expect equity markets to perform well, but after a further correction in H1 2023, due to global recession.
- We could joke and assert, it can go only on the opposite direction, but being equity markets at the crucial long term support of the 200d moving average, the FED not giving any sign of pivot and more weak fundamentals ahead, it is still to early to be fully contrarian and we still have to have drastic measures to limit the drawdown risk in case of a breakdown. We are closely following to build up a small position in put options again and we keep our stop loss at the lows of October 2022. Meanwhile Europe is surprisingly strong for the moment.



Source: Edward Jones via Syz Group

Volume of bitcoin transaction

- One very important argument for valuing bitcoin was the comparison with the volume of transaction vs Paypal or credit cards.
- On the right-hand chart we can notice, that the volume of **Bitcoin transaction during 2022 increased exponentially and therefore also the commission from transactions for miners.**
- **The volume is USD 60 trillion**
- The main crypto currencies, namely Bitcoin and Ethereum have finally stabilized, as also the all sector, after the “thunderstorm” FTX.
- In addition, it looks like, “weak hands” are out.
- Technically speaking, both Ethereum and Bitcoin set up a solid base and could finally rebound.
- Therefore it is time to slowly build up again small long positions, especially in Ethereum, which also gives some yields.



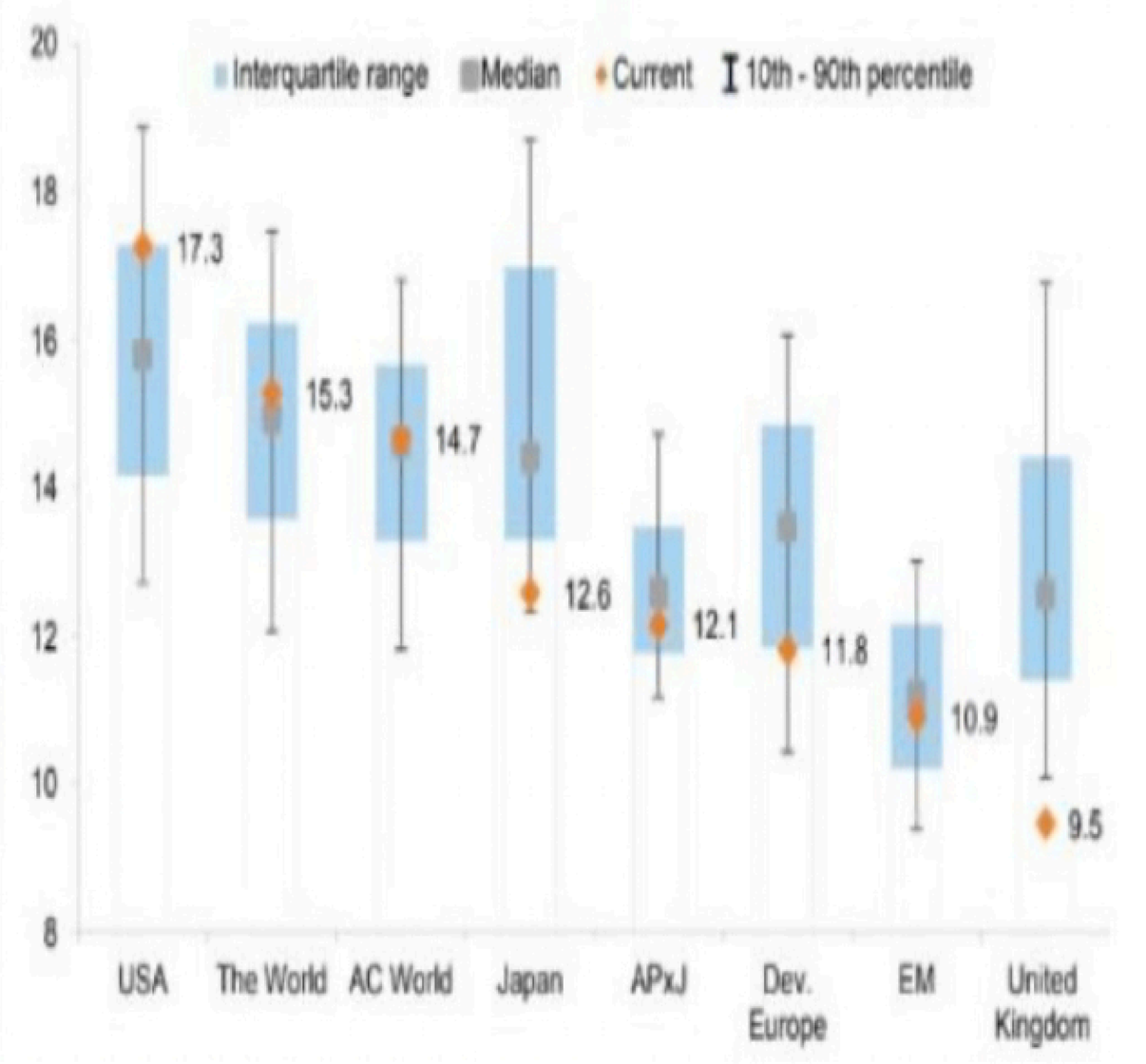
Source: Mr. Pierre Rochard via Syz group

Macro - immigration is still not an option for U.S.

- Mr Apte argued in his blog, that having 5 million gap between the labor demand and labor supply, we have to hope that the labor force participation goes up to its pre-pandemic levels, having the FED attempting to bring the labor demand down and hoping to influence also the job opening component, which are correlated. As we know, the ultimate target of the FED is to reduce wage inflation.
- As we have recently analyzed, it will not happen, that force participation will go up to pre-pandemic levels, having newly 3.5 mio U.S. citizens invalid due to Covid and many baby boomers retiring earlier.
- But Mr. Apte is also the first person, who finally questions, if an alternative strategy could be the US government policy allowing higher levels of immigration to fill the gap and being the easiest way to reduce wage inflation, especially because more than 50% of open jobs are specialists, which USA just does not have.
- On KTS's question, why the Biden's administration is not reacting faster, being the only logical solution, Mr. Apte answered, **immigration is still a very sensitive subject for U.S. citizens** and therefore the U.S. government is still not ready to change policy.
- It is a fair point and therefore we have to seriously start to ask ourselves, if the U.S. government prefers to have the economy in a deep recession, rather than open up boarders with a target immigration, which could be only healthy.
- **Equity markets are in fact, still not at "safe" levels and we have to be extremely careful on the consolidation at the 200d moving average for both the S&P 500 Index and the Nasdaq Index. If US equity markets are going to collapse, the world will follow,** even we must admit, European equity markets had a strong start of the year vs. US indices.

UK equities are valued cheaper than emerging market equities

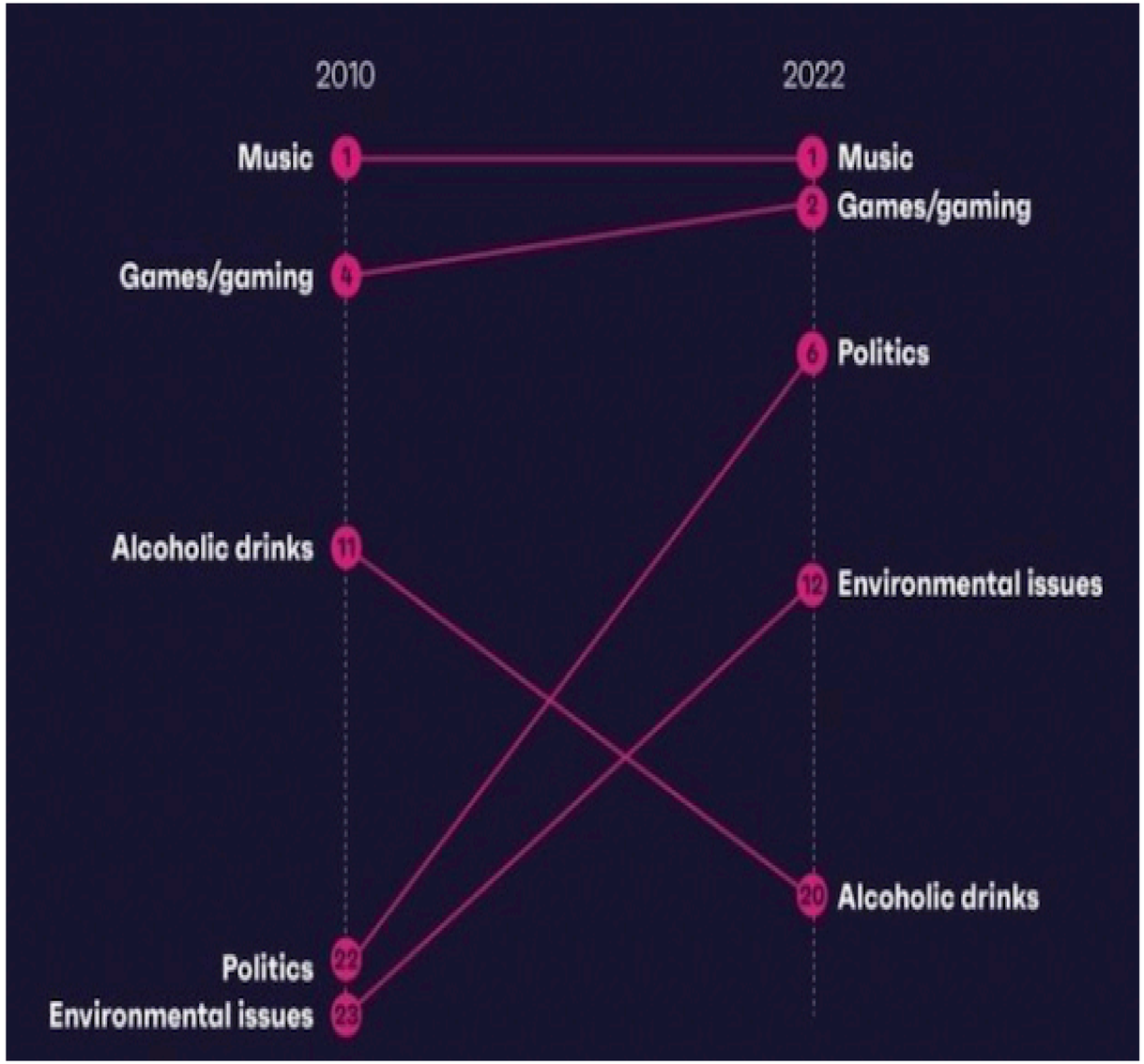
- We would like to include again the chart showing how UK equities valuation is at multiple 9.5x (12m forward P/E) and therefore lower than Emmas (10.9x).
- We find an investment into the etf of UK mid caps (MIDD LN) attractive.
- We believe, UK could have some fundamental positive triggers during 2023 and technically speaking, the mid caps index consolidate very well, therefore it could be reading for a short term breakout.



Valuation range (MSCI regions) over 20years (source: GS)

How young people have changed

- We include an interesting chart, courtesy Mr. Tangen, where we can notice, that youngsters (survey in US/UK among 16-24 year olds on online subjects) are drinking less, but caring about environmental issues and politics, meanwhile music and gaming are still at the top.
- We welcome the fact, that young people want to change the world for better and it shows to KTS, that we have to keep focusing on the mega trend “green transition”.



Source GWI Core

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