# Incrementum All Seasons Fund

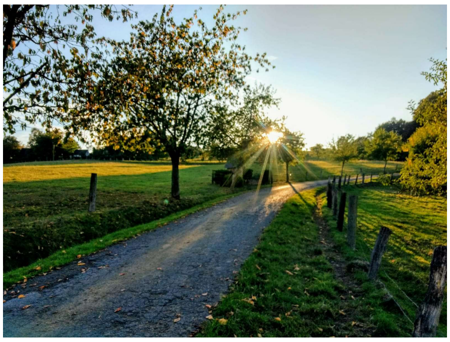
*– in pursuit of real returns –*

Source: Harvest time (HGS own pic)

*November 2019*

***Seasonal Reflections***

Fall



Source: Autumn view from my parents' house (HGS own pic)

***Quote(s) of the Month:***

*"What does the economy or money in the modern day world actually mean, is it real or simply an illusion?*

- *We look at prices on an exchange to reckon value, having failed to see that wealth creation via the stock market does not create resources in the economy. We don't see that booming markets without savings is not an accumulation of resources but an accumulation of claims on existing resources.*
- *We hail growth by looking at a meaningless aggregate such as GDP and we hope for higher prices, dismissing the fact that such aggregate growth in money terms more often than not comes from debt creation and the consumption of our capital. Yet we reckon all this as a modern financial miracle.*
- *We have abolished the idea of failure — nature's cleansing mechanism. As a consequence, we've lost real economic vitality. We've substituted finance for an industry as the locomotive of economic growth. In GDP terms, it looks terrific. But it is neither enduring nor real.*
- *A promise to pay is not money. We dress it up as a bank deposit, a treasury bill or some variation thereto and insist on calling it an asset. But we also laugh at the man who chooses to keep his cash in gold. The price of something becomes our value determinant rather than its characteristics in being real, enduring, or suitable as a means to our objective. …*
- *We have substituted the law for what is moral and what is right. We have substituted audit checklists for an auditor's judgment about what is true and fair. And we have substituted phoney mathematics for the judgment we once possessed in understanding the nature of value and that of risk."* (Source: Excerpts from https://www.investorsingh.com/40-invaluable-investing-lessons-from-tony-deden/)

*"We also had investors salivating over the prospect of the baton being passed from monetary policy to fiscal policy, which was the theme at the weekend IMF and World Bank meetings. No mention, mind you, of how the global economy is choking on too much debt as it is."* (Source: Espresso with Dave, Gluskin Sheff, 21.10.2019, P. 3)

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Dear Reader,

October has launched the darker side of the seasonal cycle, where on our side of the globe the days are turning noticeably shorter than the nights. It is still a beautiful month, witnessing the grape harvest before the first frosts arrive and when the leaves are changing colour and begin falling.

The first day of October I had the pleasure attending a luncheon with Friedrich Merz, who last year was narrowly defeated in his quest to become Chairman of Germany's largest conservative party CDU, and who is still regarded by many as most suitable future German chancellor. Despite of the meaty title of his speech *"Aufstehen"* (English: Get up), it turned out a rather balanced yet far-ranging affair, touching on major European and international policy subjects, made by a politician who came across not only rhetorically superb, but also candid, honest, convincing and well versed in the many political themes that demand being addressed. – I cannot believe that Germany could do worse with him at the political helm.

Later that day saw all five Incrementum partners gathering for a strategic offsite in nearby Montafon, Austria, where over the course of the following two days we discussed our plans for Incrementum as a boutique research and wealth management firm. I enjoyed this event a lot, as it helped us partners to get to know each other better still, while it also revealed that despite the occasional difference in opinion on individual matters, we are broadly sharing the same goals and values.

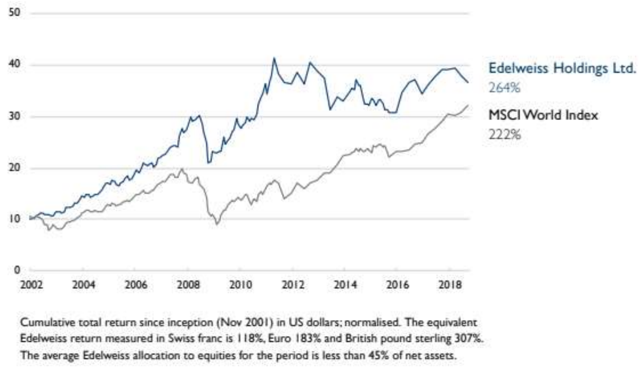
As one result and following a few hours of vivid discussions on who we are, and what we stand for, we narrowed down our choice of corporate claim to **Incrementum: Authentic Investment Partners**. Reliability, Honesty, Integrity, Out-of-the-box Thinking, etc were other shared claims / convictions, but we found Authenticity and Partnership most important in our dealing with all stakeholders of the firm. Clearly, these characteristics have always formed the bedrock of my work with clients and investors, and thus this represents an entirely suitable claim, which has yet to be finally agreed upon though.

The following week my mum, aged a mere 74, passed away following an almost year-long battle with an aggressive form of cancer. She had always been a strong and determined woman, who hand-in-hand with my dad had built up the family farm to one of the largest in the region I come from.

She was both smart and hard-working, with an entrepreneurial spirit, and proud of her life's achievement. The cancer took away the control she had always felt in her life, and in the end – though she did no longer suffer much pain - she was reduced to such a state of frailty that she could no longer bear it herself. Withered physically and mentally, she finally passed away on October 8. – Another leaf fallen….

Following an incredibly sad and yet also concluding funeral one and a half weeks later, life has resumed some degree of normality over the last 10 days of the month, which saw me begin writing these pages. And having been confronted with one of life's starkest realities, I find myself with even less patience and understanding for the detached manner in which investors seem to regard the world's present circumstances. My current mood may help explain the two opening quotes, which as usual in this space I found worth sharing with my readers.

The lengthier one represents excerpts from *"40 'invaluable' investing lessons from Tony Deden", who* is Chairman of Edelweiss Holdings, a holding company with approx. USD 300m in shareholders equity. Tony Deden is rightfully admired for his principled investment approach, though he has had a bit of a challenging time generating alpha over the past eight years. And yet I am sure he will have stuck with his investing lessons, of which the above selected resonated most strongly with me.

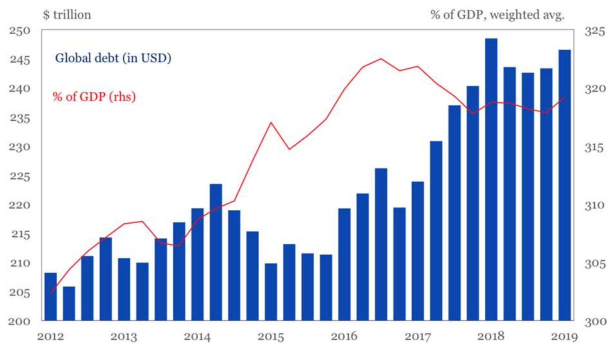


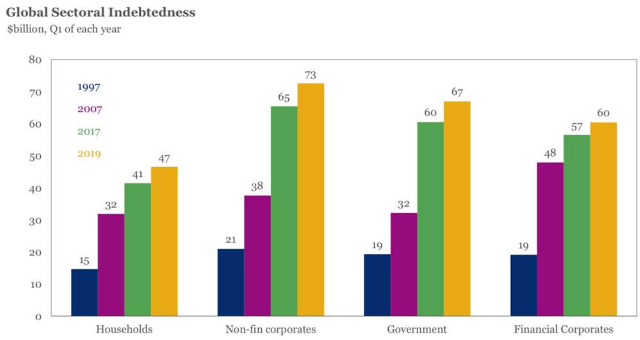

Source: https://edelweissholdings.com/docs/EH-2018-10-Corporate-Presentation.pdf

The shorter quote meanwhile reflects my frustration about financial (and in particular equity) markets, who cannot seem to find anything negative about an underlying fundamental environment that quite frankly scares the hell out of me… – **I will briefly try to summarize it with the following points**:

- Over the past more than two decades, **the world has witnessed increasingly interventionist economic policies**. Monetary policy has become the primary tool to smoothen out economic cycle contractions, a policy approach also known as Greenspan Put.

- This has led to a **growing manipulation of** the most important price in the global economy, i.e. **interest rates**, towards and below the zero bound, which as a consequence **has fuelled massive debt accumulation** both in the private as well as the public sector.



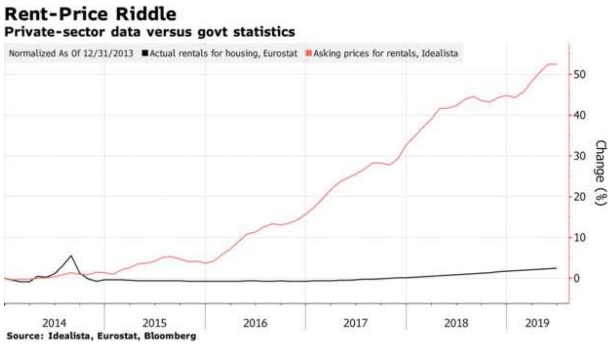

(Source: https://www.iif.com/Portals/0/Files/content/GDM_Aug2019_vf.pdf)

- Nevertheless, **goods and services price inflation has been well behaved** and given rise to the theory that inflation is dead, or at least permanently subdued due to technological advances / productivity growth, an ageing world population, and the integration of the developing world workforce into global manufacturing and supply chains. I certainly do not agree with that conclusion, and instead regard such headlines as a typical contrary indicator, as we often find them at the turn of major trend shifts. (Another example would be "The Death of Equities", famously proclaimed by BusinessWeek in August 1979.)


Source: Businessweek, April 22, 2019

Instead, I am convinced that inflation is not dead, but that we have failed to measure it properly, with more evidence showing up in the media, e.g. https://www.bloomberg.com/news/articles/2019-10-17/rents-cost-less-than-tents-in-europe-s-twisted-inflation-data

Using the example of Spain, the article deals with rent and house price inflation in the EU, and how this is not sufficiently reflected in common price measures like CPI (Consumer Price Inflation). To quote: *"In Europe there are no private figures on housing costs for government statisticians to use as a comparison, and somehow they have become minimized in inflation readings in Spain and many developed countries. … Asking prices for rent jumped 50% nationwide in the previous 5 1/2 years, the research showed. Government statisticians figured housing costs rose barely 3% in the period."*

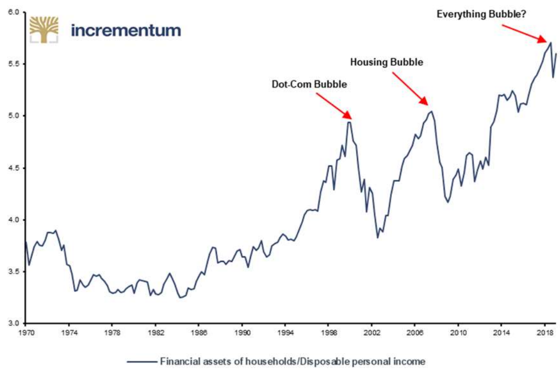



Let me reiterate this: **The biggest expense for average private households, which generally accounts for 30-50% of disposable income, has actually risen by 50% in Spain over the last five and a half year, but Spanish CPI only accounts for a mere 3% of that in its composition…** - This should help solving the riddle of the growing wealth divide, and lacklustre economic / demand growth…

The article continues: *"A spokesperson for Eurostat, which compiles price data, said that while revising the inflation index to capture more housing costs was considered and rejected in 2018, "research will continue." An ECB spokeswoman declined to comment.*

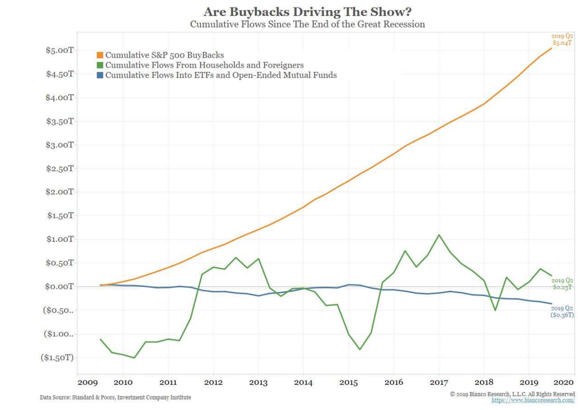
*Eurostat calculations assume consumers spend more on water, power and gas than they do on their rent. In Spain's case, it implies a household with 2,000 euros a month in disposable income pays only 60 euros a month in rent."* – To me that is a prime example of ivory tower economics at work, and a clear reason for voters in the developed world turning increasingly away from the political centre, which apparently is unable to see that the rent must be paid, no matter what the reported inflation numbers…

- In addition, **monetary policy at the zero bound is no longer working**. Since the GFC central banks have increasingly resorted to large scale asset purchase programs, aiming to
a) reduce long-term interest rates and
b) create a wealth effect, with the ultimate goal to stimulate global demand. The first was achieved, but the second clearly and empirically not; instead, the targeted inflation has shown up in global asset prices.



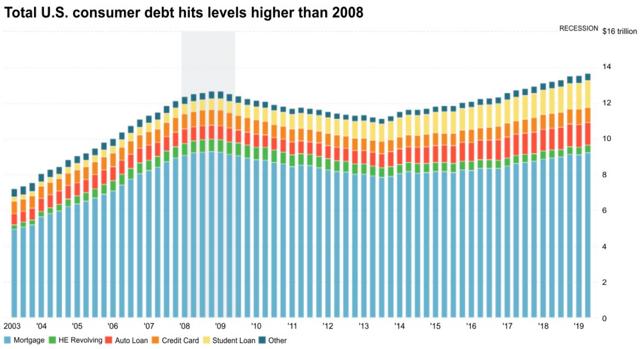

- In the process **central banks have been crowding out the private sector from safe government bonds** and are thus urging them to increase investment risk in order to maintain expected and required yield levels, while at the same time implicitly supporting an overleveraged public sector from falling into bankruptcy.

➢ Consequently, the **private sector** took advantage of ever cheaper funding cost **to increase leverage**, whether in consumer credit or to fund a growing wave of share buybacks. The latter actually represents a giant equity-for-debt swap and is often underestimated in size (including by your humble scribe). Taking the S&P500 as example, index constituent companies have been buying back USD 5 trillion of stock since 2009, which dwarfs the cumulative flow of funds from mutual funds and / or ETFs.




https://moneymaven.io/mishtalk/economics/cumulative-funds-flows-and-5-trillion-in-stock-buybacks-clJuhbHBI0iowB0Xo0lfTw/

For those who are interested in an excellent illustration of what is going on with share buybacks, please allow me to point out the following link: https://www.epsilontheory.com/yeah-its-still-water/#.Xbb_TFWGvTg.twitter, which is a must-read.




Source: https://latest.13d.com/debt-burdened-consumer-us-economy-88fe1506cbd9

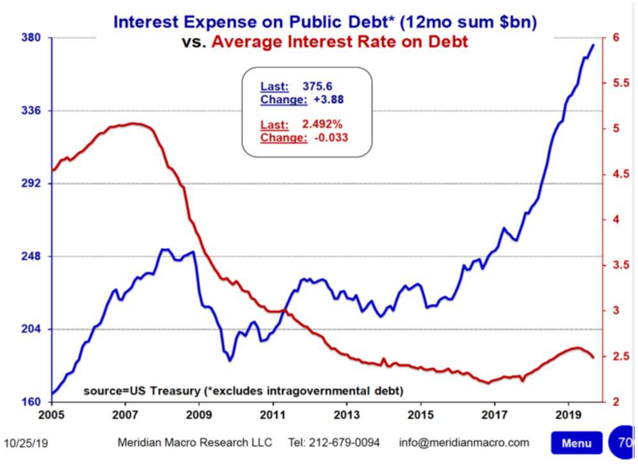
Meanwhile, the state of consumers (e.g. in the US) is aptly described in a recent piece by 13D-Research. To quote: *"Not including mortgages, millennials now carry an average of $27,900 in debt, according to analysis released by Northwestern Mutual last month. For Gen Z — the oldest of whom are still only 22 years old — that number is an incredible $14,700. As for baby boomers, they have just under $137,000 saved for retirement on average, far less than needed to support current spending."*

How does the average US consumer retire on USD 137,000 in savings, which on a risk-free basis earn them the stately amount of approx. USD 2,740 p.a. (based on 2% yield)? – This is only one of the unintended consequences (or perhaps wilfully accepted side-effects) of the unconventional monetary policy of the past decade, which initially was merely supposed to ward of a crisis but has long become standard operating procedure, penalizing savers and wrecking an entire retirement system in the process.

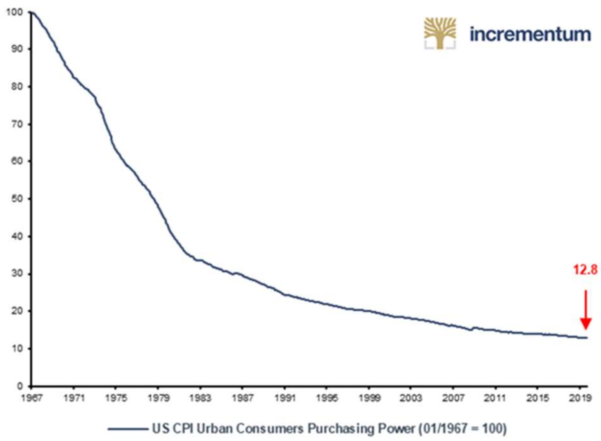
➢ With this failure of monetary policy to achieve its stated goals there are **increasing calls for fiscal policy to take over**. This includes concepts like MMT (Modern Monetary Theory), which advocate increased fiscal spending via further government debt accumulation which in turn is funded by central banks' monetary expansion. Few democratically elected politicians will be able to resist the siren call of more fiscal spending, and thus the already overwhelming debt load will continue to expand.

➢ **We ultimately expect this to lead to an increasingly inflationary environment**, as government spending (be it on social security, more employment, or large-scale infrastructure investments) ends up creating new credit-funded demand for goods and services. Besides, the inflationary path is the only one that lowers the real burden of debt in society, reducing the need for large scale bankruptcies and write-offs, although it is designed to and will greatly reduce savers' purchasing power.

Here it is important to realize how far the world has gone already. Taking the US example, the interest expense on public debt keeps climbing despite of interest rates having nearly halved over the past 12 years. For a while, the institutional depression of interest rates helped carrying ever larger debt burdens at a stagnant or even declining total cost. But with the debt-berg continuing to grow and interest rates already at / near record lows, interest expenses are likely to grow further. How dire the public funding situation has become is evident in the Fed's recent U-turn concerning its planned balance sheet reduction.




Source: "Things that make you go hmmm", 27 October 2019




Can the authorities force savers to accept negative interest rates forever? – Given that time preference is inherently positive, i.e. receiving something today is preferable to receiving it tomorrow, history suggests that savers will rather spend the money today than receive less in future. For now, households still trust in the narrative that inflation is low and will be low for years to come, all factual evidence to the contrary (see chart on the left) notwithstanding. – And yet they begin to wonder why the purchasing power of their disposable income keeps deteriorating?

In my view this is one of the main reasons for the spreading of social unrest and protests erupting in societies around the world. When reality dawns on enough people, trust in our established monetary system will be shaken to the core and lead to a reset, which will be painful for many people.

For now, however, markets continue to float on plenty of hot air, as they have been turned into political utilities, where the level of the Dow / S&P500 determines whether the economy is doing well, while according to the US Census Bureau 40m US citizens are collecting food stamps and an estimated 50% of Americans are receiving at least one federal benefit...

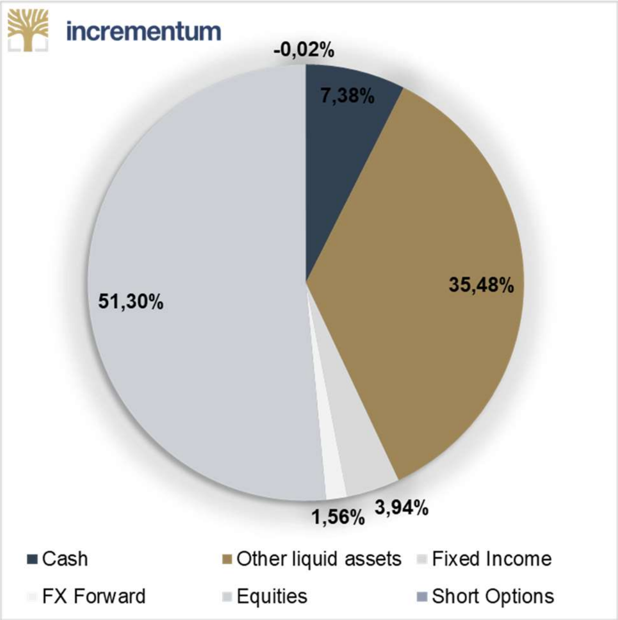
Clearly, an appalling state of affairs, which I remain convinced will prove unsustainable in the longer-run.


https://app.hedgeye.com/insights/78776-cartoon-of-the-day-coked-up-bull?type=cartoons

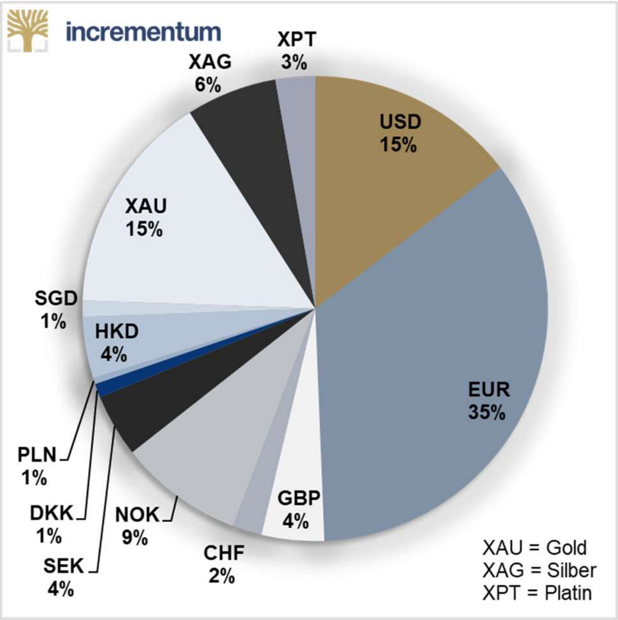
Hence my goal and focus as manager of the **Incrementum All Seasons Fund** is to maintain a cautious investment stance, in order to prudently navigate investors assets through this difficult, challenging and truly disruptive period. After all, **'The key is not to predict the future, but to prepare for it.'** (Pericles 500 BC)

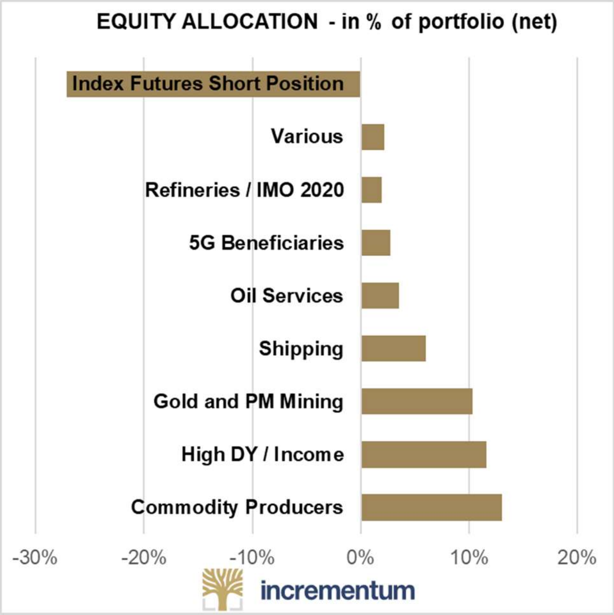
# IASF – October 2019 Review and Comments

## Asset Allocation




## Currency Allocation




In October, IASF's gross equity allocation rose by 4% to 51%. Some profit-taking on trading position was overcompensated by new investments made in Osisko, John Wood, Nokia and Man Group.

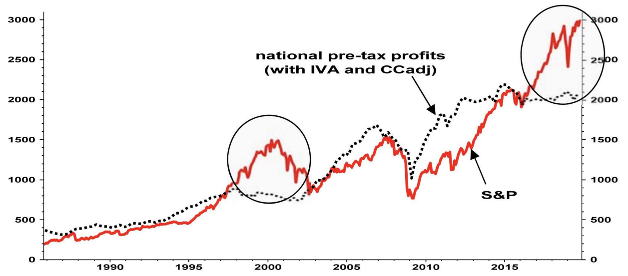
FX allocation was barely changed, apart from a small reduction in USD towards PM investments. USD exposure currently sits at 15% of the portfolio, consisting mainly of commodity and other USD based businesses like shipping and refineries, which in a weaker USD environment should do well. Meanwhile, IASF's precious metals exposure (physically backed ETCs and miners) has been further increased and now amounts to 24% of the fund.

IASF's short positions remained unchanged, currently amounting to about 27%, with an additional 7% hedged via S&P500 put options. Despite of last week's risk-on move, which saw the S&P500 make a new all-time high, we continue to believe that the so achieved reduction in overall equity market risk remains entirely appropriate, as financial markets move in cycles and this particular one is without a doubt extremely stretched.

## In Closing

There are many issues that should concern investors, whether it is the accelerating polarization in Western democracies, a potential impeachment of the US president (see also: https://www.theguardian.com/commentisfree/2019/nov/02/its-time-to-throw-the-kitchen-sink-at-trump-impeachment), the ongoing Brexit drama, a global economy that is weakening (including slowing growth in China), or the lack of profit growth in the listed corporate sector while its balance sheet is deteriorating.

**The S&P has become totally detached from underlying profits – just as it did in the late 1990s**




Source: Datastream

Source: https://www.marketwatch.com/story/carnage-awaits-investors-if-this-chart-is-anything-to-go-by-2019-10-28?mc_cid=19ba2ffe6d&mc_eid=752dd6c786

The authorities have responded in predictable fashion, whether it is to the recent problem in the US repo markets, where a liquidity crunch caused repo rates to temporarily spike to 10% last month, which in turn has caused the Fed to completely reverse its policy by resuming large scale asset purchases again, or the ECB's Mario Draghi's final parting rate cut and attempt to resurrect its own asset purchases, which the Financial Times commented on as follows:

***"Ironically, the Fed is reluctant to call its balance-sheet expansion quantitative easing, while the European Central Bank is embracing QE with no guarantee it will expand its balance sheet. When the cavalry turns up like this, reluctant and dishevelled, there is no reason to believe it will be a particularly effective fighting force."*** (Source: https://www.ft.com/content/998f5176-f9ac-11e9-98fd-4d6c20050229)

With so much uncertainty, coupled with historically elevated valuations and increasingly ineffective monetary policy tools, **IASF's** cautious positioning is entirely adequate. It is also worth to point out that if monetary policy is losing its potency, gold (and its precious metals peers) may gain a broader appeal again among investors as effective portfolio diversifier. This especially as low to negative interest rates reduce the opportunity cost of holding gold, and the increasingly politicised environment suggests that the authorities may well favour currency debasement as a tool to gain competitive advantages.

As usual I am happy to discuss any of this in more detail with investors.

Greetings from Schaan, Liechtenstein!

**Hans G. Schiefen**
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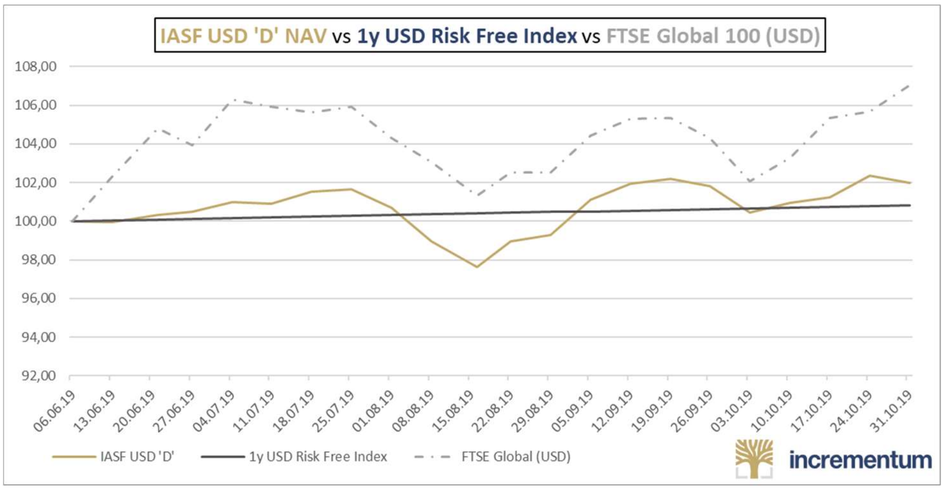
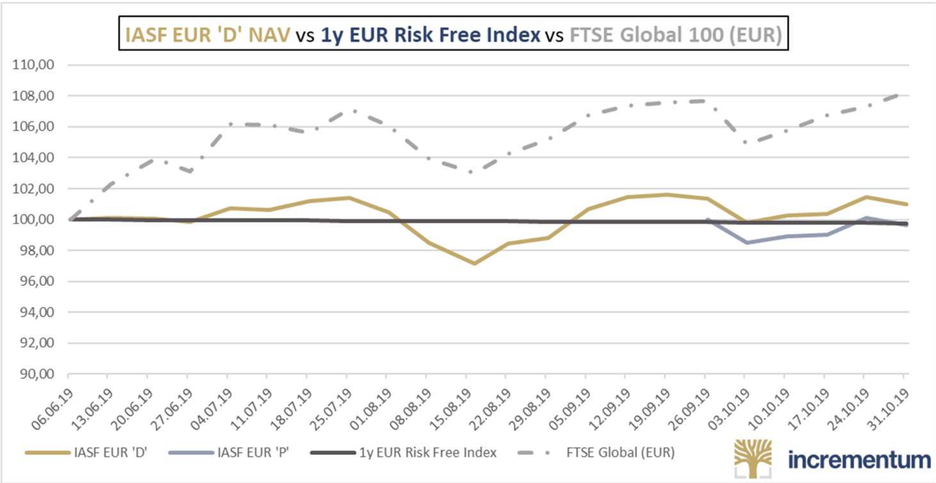
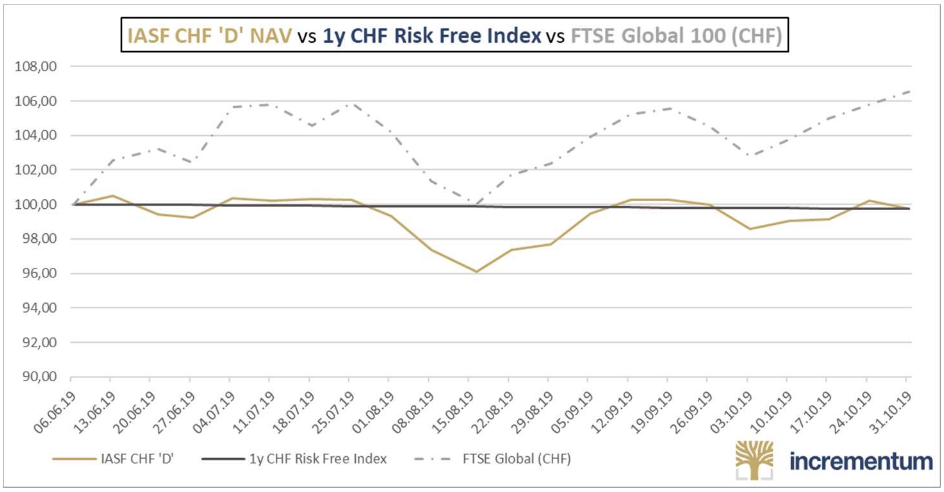
## Appendix *




* Graphs display NAV of IASF 'D' shares as of last valuation date (**31Oct2019**), compared to the respective risk-free 1y-government yield as well as the FTSE Global 100 Index in respective currency as a proxy for overall equity market performance, from the start of the investment period (6Jun2019) on an indexed basis.

## IASF PM Shaped By 8 Investment Lessons

1. Capital markets, like the economy, are inherently cyclical in nature, and you must always know where you are in the cycle, while not hesitating to "Be fearful when others are greedy and greedy when others are fearful." (Quote: Warren Buffett)
2. Prices paid determine future returns, i.e. the higher valuations are, the lower future return expectations must be (and vice versa), which is the essence of value investing.
3. Capital preservation is the conditio sine qua non, and a consistent and long-term investment strategy is more important than short-term momentum chasing.
4. As a result you must always know when you trade, or when you invest.
5. The most basic and effective risk management tools are proper diversification and the ability to hold cash.
6. Hard assets are preferable to intangibles, distributions to accruals.
7. Look for the incentives: True alignment of interest works in investors' favor.
8. There is no magic formula for successful investing: Consider both macro- and micro-economic issues, be diligent, flexible, patient, keep an open mind, and realize that investing will always remain more of an art rather than a science.

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