Incrementum All Seasons Fund

– in pursuit of real returns –




2022 / 05

Seasonal Reflections

Tough markets

Dear Reader / Investor,

Autumn has arrived, and despite of the increasing shortness of days, it is still a beautiful season. Today's seasonal pics were made at the Old Rhine (Alter Rhein) around Diepoldsau (CH), where Alexandra and I went for a leisurely Sunday walk in October.

Old Rhine in autumn, 23OCT22, HGS pic

The Old Rhine is part of the historic rhine riverbed in the Rhine Valley of St. Gallen and Vorarlberg, which was cut off when the course of the river was straightened as part of the Rhine regulation.

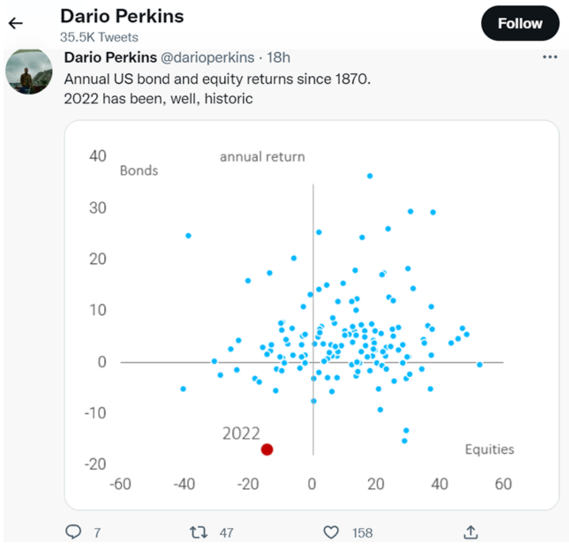
Old Rhine in autumn, 23OCT22, HGS pic

During a rather busy autumn, I highly appreciated the tranquillity of our hike, which also showcased the beauty of the unregulated river in stark contrast to its regulated parts. (The accompanying aerial shot may serve to illustrate the said contrast, and no, it does not get any more exciting closer up.) – Having worked my entire life in an ever more tightly regulated financial services industry, there are clearly parallels here…

Luftbilderschweiz.ch

But, of course, this is an investment letter, and not a place to vent my frustrations about the consequences of seemingly ever-increasing government interference in the private sector, a subject on which most readers will have their own views, anyway. Thus, let's jump right into the investment stuff, and check out the two graphs below, which neatly summarize the investing vintage of 2022:

The Macro Tourist Private Twitter Feed Recap, 11OCT2022



@darioperkins, Twitter, 31OCT2022

As the BofA graph above on the left shows, a balanced investment portfolio consisting of 60% S&P500 and 40% 30-year US-Treasury bonds over the first nine months of this year experienced the worst drawdown (-27%) in a century. For an equivalent perspective, the Euro STOXX 600 Index lost 20.5% and the 30-year German 0% Bund, maturing on 15AUG2052, a staggering 42.7% during the same period, yielding a 60/40 portfolio total return of -29%. That kind of extreme negative outlier performance is also confirmed by the scatter plot chart above on the right, which includes improved October data, and still confirms 2022 as a vintage that at best leaves a lingering sour taste.

How did that happen? – Before I attempt an answer, please do note that…

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The answer to *"How could that happen?"* is simple. Correlations, which for decades had been taken for granted and relied upon in portfolio construction, shifted. And past patterns of rising bond prices, which used to cushion portfolio downside from falling equity prices, simply broke. David Dredge from Convex Strategies in Singapore, commented on this in a recent blog post:

"It doesn't take a great mental leap to determine that a major (perhaps the major) uncapitalized tail that has built up over the last 35 years, call it the era of the "Greenspan Put", is the Sharpe World *driven universal belief and application that the Fixed Income component of the 60/40 portfolio, and all of its many variations, is RISK REDUCING! In* Sharpe World*, the Fixed Income characteristics of low volatility, bounded upside, low to negative correlation is deemed to have a portfolio benefit and reduces, in effect, the amount of capital you would otherwise deem necessary to hold against potential losses on the portfolio.*

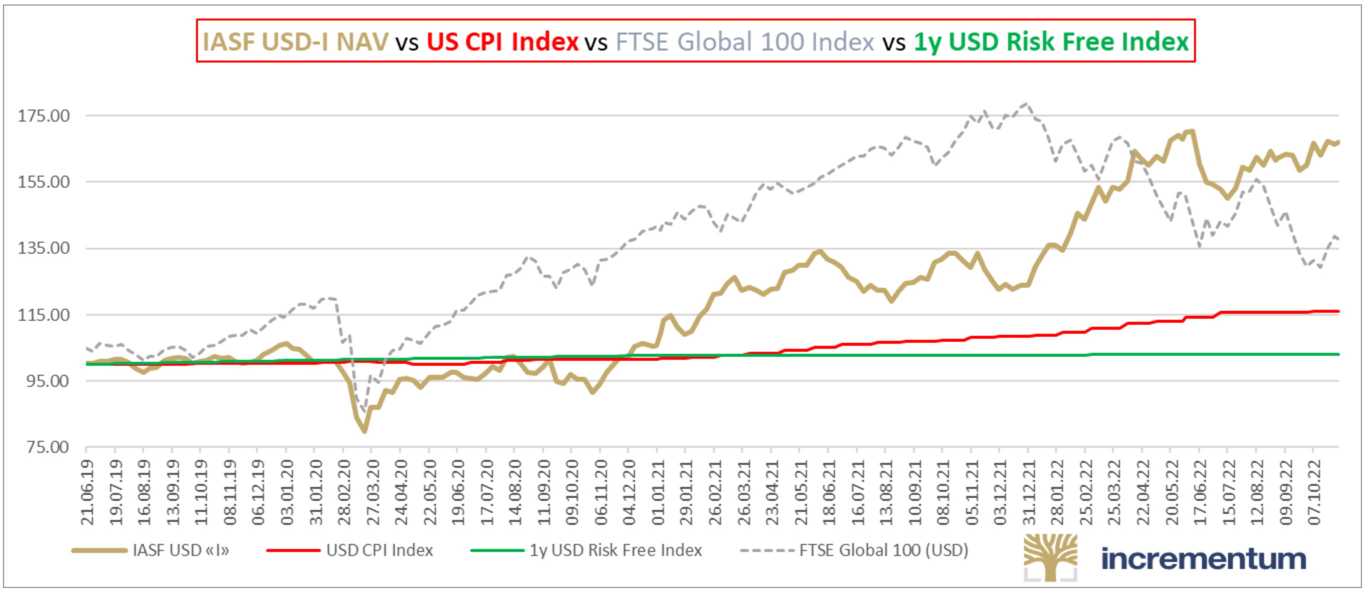
That, of course, only holds as long as the Sharpe World *assumptions of low volatility and low/negative correlation to the other portfolio components persists. Those beneficial components have persisted for a reasonably significant number of years, but notably aided and accentuated through active manipulation by central bank policy makers through ever greater interventions to drive yields lower and to suppress/curtail volatility, particularly around events that necessitated the negatively correlating response. That is not currently the case. …*

When the assumptions of low volatility and negative correlation fail, the magical 60/40 loses its lustre." (Risk Update: September 2022 – Is "Sharpe World" Closing?, Sep 2022)

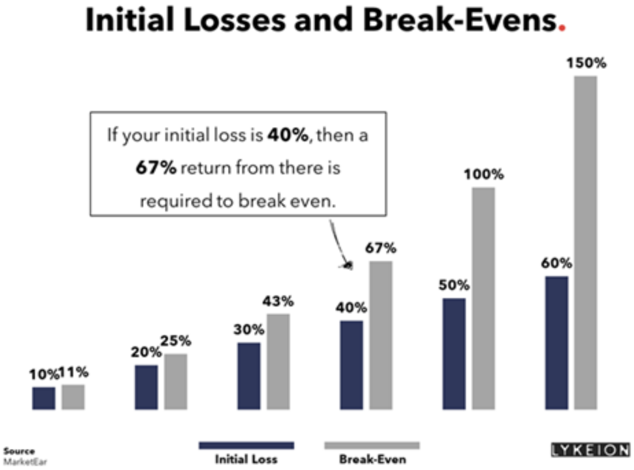
I am not here to boast that I saw all this coming. Indeed, I had been cautioning investors to expect something like this for some time now, which probably would have caused an old Aussie friend of mine to remark *"Even a broken clock is right twice a day"*. Over those years, my more cautious risk positioning, value bend and absolute return focus were not a recipe for (equity market!) outperformance, as one had to compete with passive investment managers that offered (often leveraged) beta to the lucky investor who so smartly rode these trends. - But 2022 has made up for this and then some.

Marked by a similar experience, one of the last remaining value investors, David Einhorn, was quoted last month with the following statement: *"Value investing? – I don't know that it ever comes back! – You know, there have been serious changes to the market structure, and pretty much most of the value investors have been put out of business."* (Bloomberg, 11OCT2022) - This was widely regarded as an obituary on the value investing discipline. But instead, and as clarified in a subsequent interview with Grant Williams, his statement was rather based on his observation of how the structure of the investing industry had shifted from active (and predominantly value driven) to passive (and thus index-linked). As a result, there are far fewer analysts to evaluate individual companies, and few investment managers left, that pursue a truly active, value-driven and benchmark independent investment management approach, which actually makes this a fantastic time to have skill in this area.

And so, I cannot help but feeling vindicated by the events this year, which for **Incrementum All Seasons Fund (IASF)** investors has turned out an extraordinary year. Many of them chose in 2019 to entrust their money to **Incrementum**, and its newly launched **IASF**, rather than keeping it in risk-free investments. They did this with faith in **Incrementum** as well as me as responsible fund manager to deliver on our objective to achieve real, i.e., inflation-adjusted, growth in the value of invested asset over the market cycle, and consequently to expand their purchasing power. As the graph below shows, we have succeeded in a manner that has not only significantly beaten the performance of any kind of 60/40 portfolio, but also global equity markets, and all of this on a net (i.e., after all cost) basis.



In over three decades as professional investment manager, I have learned (early on even in the best, which is the hard way) the importance of avoiding major losses. The graph on the right tells the tale: The more dramatic the decline in one's portfolio value, the bigger the subsequent gains required to get back to break-even. Protecting one's downside is particularly important when markets are clearly expensive. And this they have been for quite a few years prior to 2022, a subject on which I have regularly commented in these pages.



Bear Markets: How to Identify a Bottom, Lykeion, 10NOV2022

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As of the time of writing these lines, equity and bond markets have been experiencing another rally from their prior lows, and it appears that investors are growing confident again that the worst is behind us in this cycle. Is that the case, and thus time to get aggressive again in investment allocations?

Let's try and evaluate this by looking at the macro backdrop. The OECD in its Global Economic Outlook from September, titled "Paying the Price of War", described it as follows:

"The world economy is paying a high price for Russia's unprovoked, unjustifiable and illegal war of aggression against Ukraine. With the impacts of the COVID-19 pandemic still lingering, the war is dragging down growth and putting additional upward pressure on prices, above all for food and energy. Global GDP stagnated in the second quarter of 2022 and output declined in the G20 economies. High inflation is persisting for longer than expected. In many economies, inflation in the first half of 2022 was at its highest since the 1980s. With recent indicators taking a turn for the worse, the global economic outlook has darkened.

The four main takeaways are:

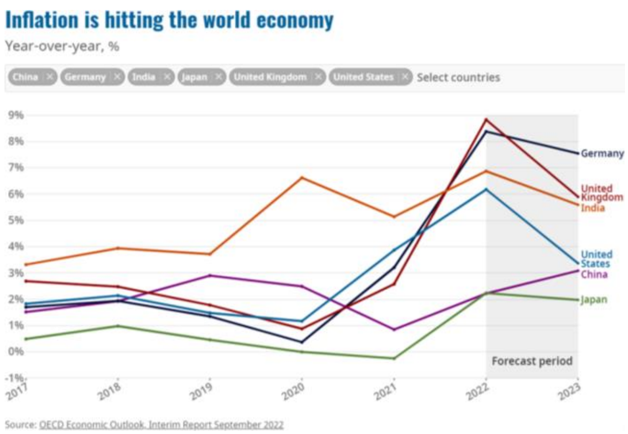
> The world economy is slowing more than anticipated

> Inflation has become more widespread

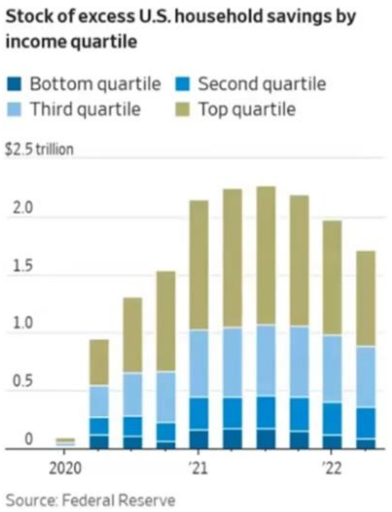
> Inflation will ease but remain at high levels

> Demand reduction and supply diversification are needed to avoid energy shortages"

Apart from the nauseating attempt to shift the blame for the world's economic woes on Russia's war in Ukraine, this still summarizes the major trends succinctly, and anyone interested in diving into more details can do so in the report. For investors, the crucial point is likely the third, as it buries any notion of inflation being transitory. This has important implications for the global monetary policy outlook and the question of timing a central bank monetary policy pivot.



https://www.oecd.org/economic-outlook/september-2022/

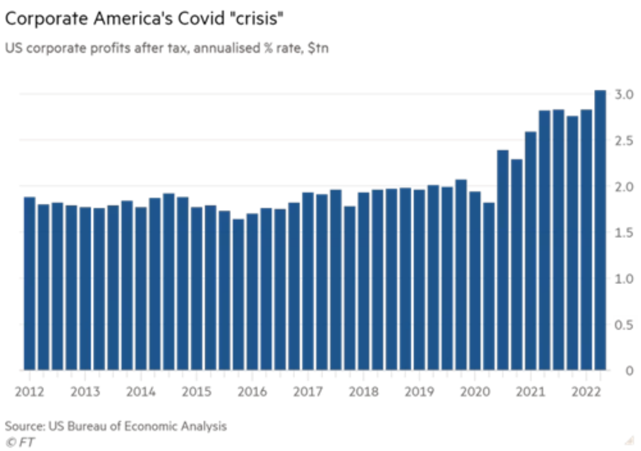


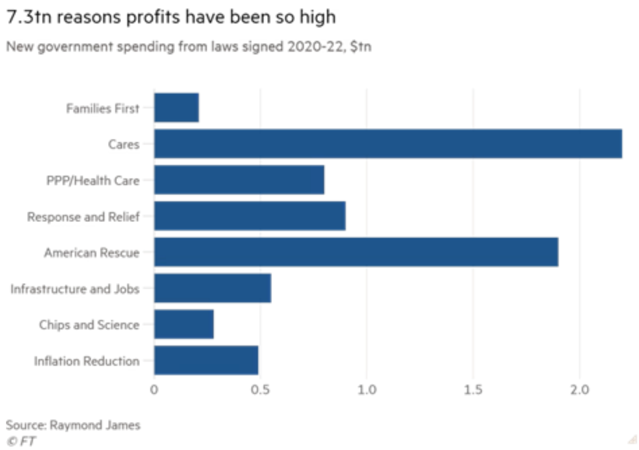
Blockworks Macro, YouTube, 1NOV2022

And all this at a time when global growth is expected to slow further, and especially developed economies are widely forecast to experience a 2023 recession.

2022 was anticipated to deliver an economic slowdown, which in the end was less pronounced than expected. The reason in my view is shown in the chart on the left, exemplifying the US situation: What has kept demand strong in real terms was the tail-end of Covid-induced fiscal stimulus, and more importantly savings that were accumulated during those Covid-marked years, which had restricted household activities and spending at the time, and have now been drawn down to plug the widening hole that is due to inflation induced loss of purchasing power.

Amid a slowing economy and a squeeze on profit margins, the corporate sector is also likely to batten down the hatches. Recent large-scale lay-off announcements even from the US tech behemoths suggests that this is already happening. Again, using US data, the corporate sector appears to have been a main beneficiary of the Covid crisis, as corporate after-tax profits rose by a third following the advent of the virus. And the FT with its graphs below also highlights the reasons:





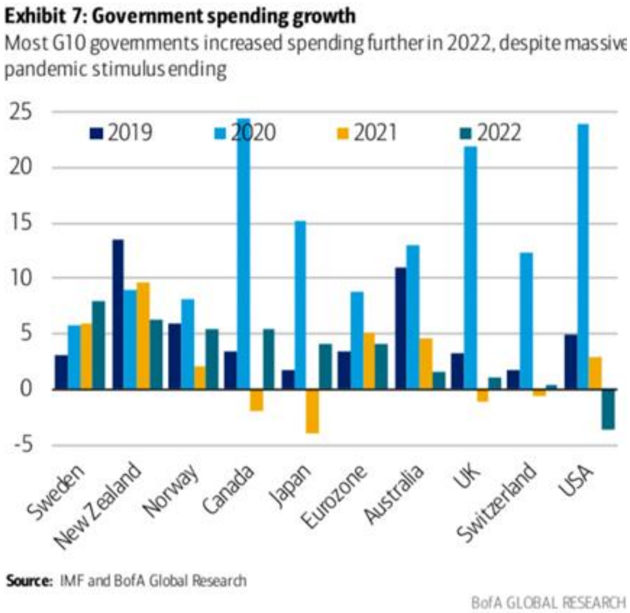
Unhedged by Robert Armstrong, FT, 2NOV2022

"Government spending, and in particular debt-financed government spending, has gone bananas since the start of the pandemic. And as we have pointed out before, deficit spending and corporate profits are closely related. The Levy-Kalecki equation (a basic accounting identity) says profits are a residual, equal to investment minus household savings, government savings and foreign savings (that is, the current account deficit). This makes intuitive sense. Savings are monies received but not spent. To make profits, companies need US households, the US government, and foreigners to spend money, not save it.

It is particularly clear why government deficit spending, which exploded during the pandemic, would be closely linked to profits. When the government borrows money and spends it, the money goes to companies either directly (think of a defence contractor) or indirectly (think of a stimulus check used to buy a new TV). Yes, when government deficits fall, there are multiple ways the US's books could balance — households and foreigners could go on a spending binge replacing the lost government largesse, for example. But a fall in profits seems to us to be more likely." (Unhedged, FT, 2NOV2022)

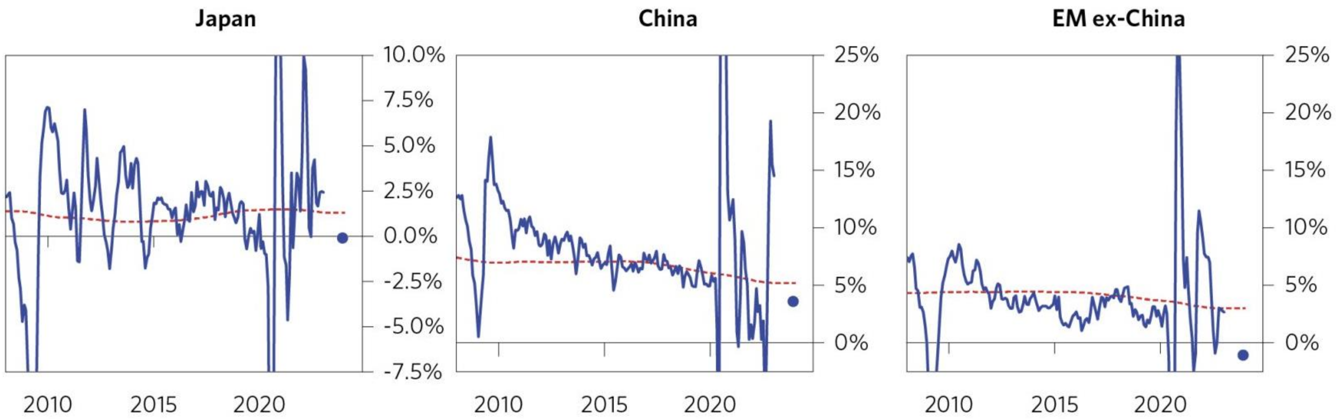
Falling corporate profits result in cost-cutting, which in turn does dampen growth. In addition, I believe a further curtailment of public spending is inevitable near-term, following the extraordinary spending wave of the past few years, as higher nominal interest rates are reminding our political class that increased debt loads result in a growing share of budgets going towards debt servicing.

So, we have consumers using (shrinking) savings to make up for the decline in real (i.e., inflation-adjusted) incomes, a corporate sector tightening its belt, and governments at least pretending to be more frugal, all suggesting a recession is likely in 2023.



Macro Tourist Private Twitter Feed Recap, 22NOV2022

A Portrait of Stagflation, Part I (Bridgewater, 10/11/22), as presented by @UrbanKaoboy, Twitter, 28OCT2022



A Portrait of Stagflation, Part I (Bridgewater, 10/11/22), as presented by @UrbanKaoboy, Twitter, 28OCT2022

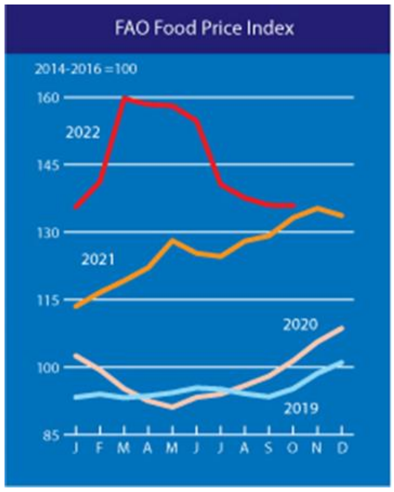
These recessionary trends are also forecasted by hedge fund giant Bridgewater Associates above, and needless to say this does not bode well for corporate profits, thus putting a question-mark behind the foundation of the recent equity market rebound.

What about inflation? – Here again, optimism increasingly reigns, as the following quote shows:

"The headlines are still screaming "food crisis", and policymakers remain worried. Sure enough, the prices of a few staples, notably corn and wheat, are still high. But dig a bit deeper, and the scare is all but over. From salmon and chickpeas to lamb and tomatoes, food prices are coming down. Deflation is now on the menu. It's a sign that global inflation has peaked." (Bloomberg's Javier Blas, 16NOV2022)

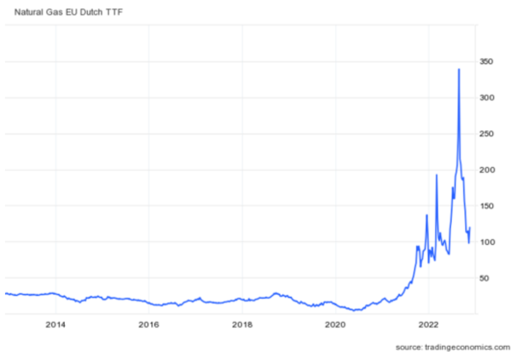
This is obviously a source of hope for inflation optimists, namely that the base effect will lead to falling year-over-year inflation rates. But if one takes a step back, this for now merely means that global food prices are stabilizing at very elevated levels.

As the graph on the right shows, the FAO Food Price Index was unchanged at around 135 in October versus September, and incidentally this reflects roughly the level first reached during Q4 2021. But what is easily forgotten when one looks merely at year-over-year changes is the absolute level of prices. And here it is noteworthy that the index, which was launched in 2014 at 100, did not break that level decisively until 2H 2020, i.e., prices are still a third higher than they were two years ago.

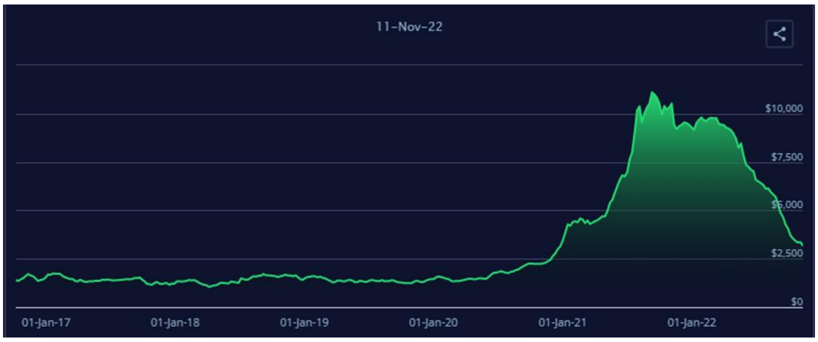


FAO Food Price Index, 4NOV2022

This is important to keep in mind, as it is a crucial issue when thinking about inflation. People tend to focus on the short-term rate of change, which is significantly impacted by the base effect following prior price rise bursts. But it is the overall price level that is more important in the longer run, a fact that is also essential to bear in mind when other price indicators are discussed, whether it is energy prices, or shipping cost.



Natural Gas EU Dutch TTF, Trading Economics

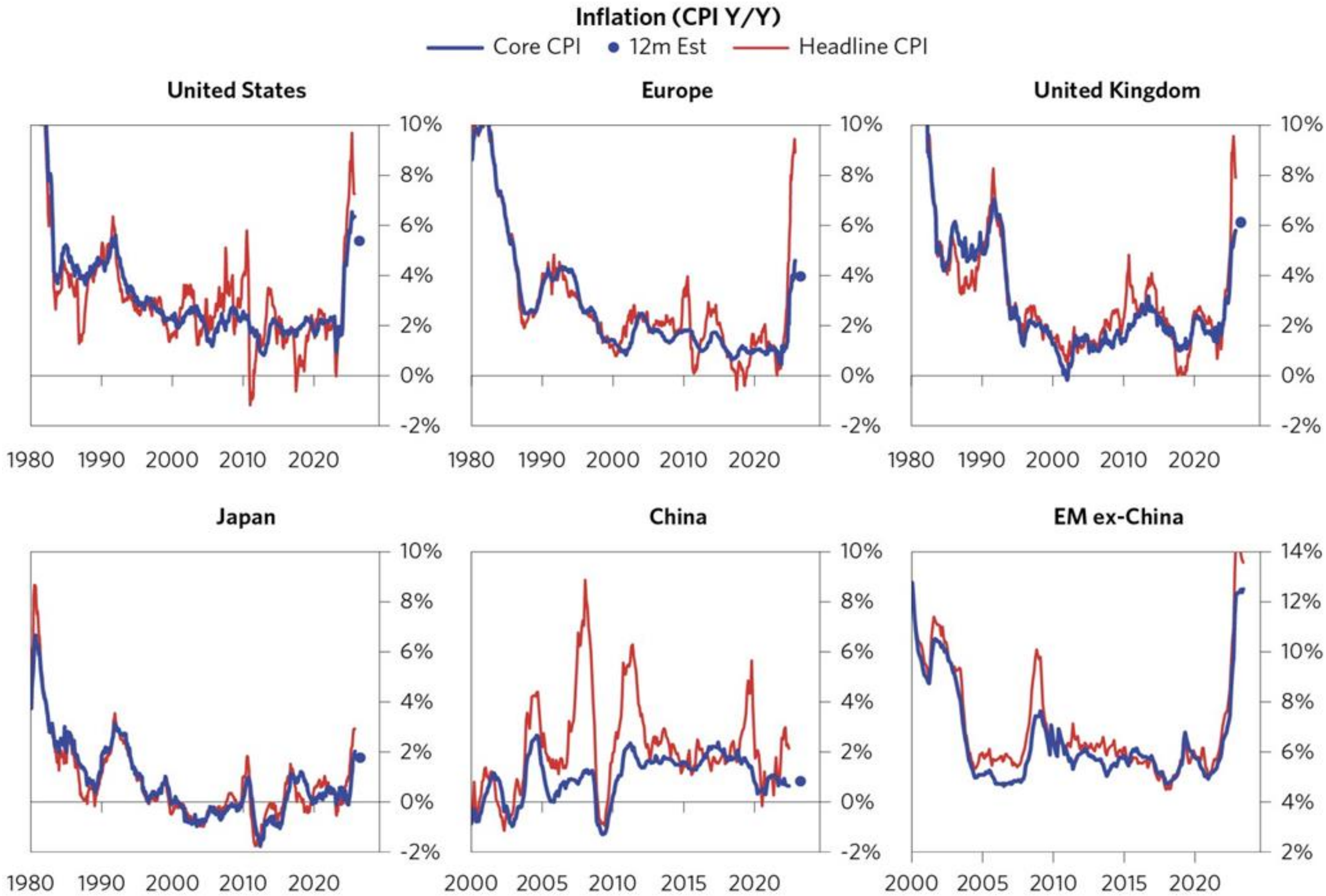


Freightos Baltic Index (FBX): Global Container Freight Index

Yes, natural gas prices in Europe have fallen two thirds from their recent peak, but they are still four times as high as they ever were in the decade prior to May 2021. And container shipping rates have fallen over 70% from their August 2021 highs and yet are still more than double their pre-mid 2020 rates. And though there has been a short-term price correction, all market participants will have to adjust to a permanently higher overall cost level, and that is also true for food. To me that suggests that overall global demand growth will be lacklustre as affordability has shrunk. But supply growth is slowing as well, as commodity supply is increasingly restricted amid a lack of replacement investment, and the manufacturing and service sector of the economy adjusts output lower to try and maintain profitability.

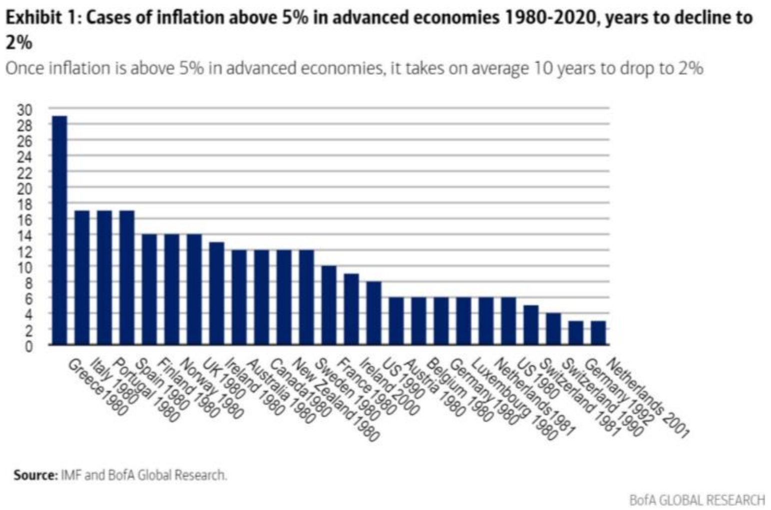
Against this backdrop, I think what most people are underestimating is how the recent inflationary burst has actually been and still is altering the mindset of all economic actors. This is because it has made the erosion of purchasing power so evident to households, while the corporate sector is faced with the double-edged knife of slowing demand coupled with still rising cost pressures.

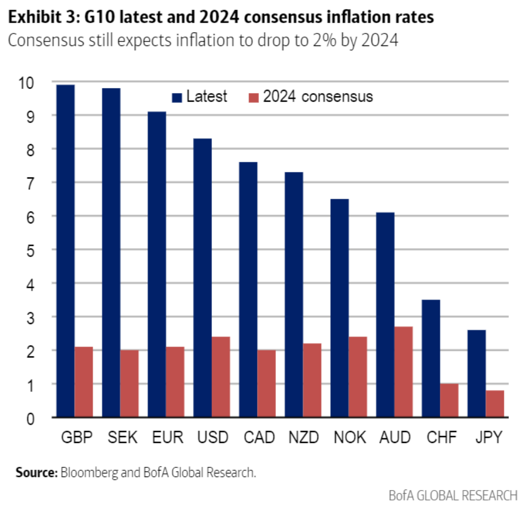
In addition, geopolitically we have entered a new era of competition rather than cooperation, with the obvious potential for conflict and as the Ukraine situation shows even war. This represents the end of an almost Ricardian era that benefited from comparative cost advantages due to modern-day just-in-time global logistic chains. Now, the realization that amid increasing geopolitical competition and restrictions in international trade we can no longer rely on uninhibited access to critical inputs for our local economies, is increasingly leading to onshoring or friend-shoring efforts, which will make these inputs more expensive. Combined with the structural force of (ageing) demographics, it is therefore hardly surprising when 12-months forecast of core inflation rates remain relatively stable.



A Portrait of Stagflation, Part II (Bridgewater, 10/11/22), as presented by @UrbanKaoboy, Twitter, 28OCT2022

In fact, history has taught us that once inflation exceeds the 5% level, it takes on average 10 years to revert to 2%, a level which economists' consensus nonetheless expects to be reclaimed by 2024.





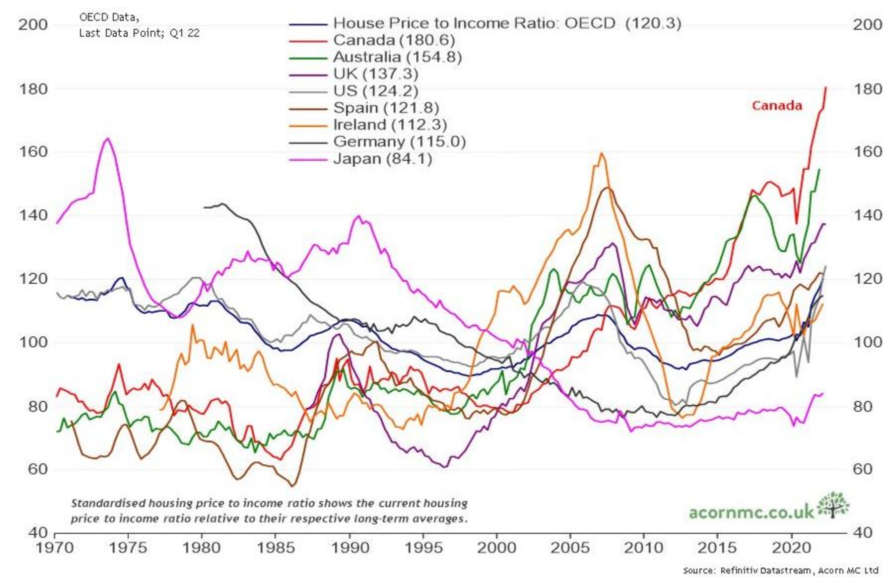
John Authers, Bloomberg, 22SEP2022

One of the main reasons for higher inflation for longer is individual households (i.e., the labour force) striving to regain their prior purchasing power levels, while governments at least in Western democracies will be eager to support them in their quest, in order to stay in favour to be re-elected. Hence, I expect that year-over-year inflation rates are going to ease in 2023, but it is highly unlikely that we will revert to 2% inflation rates or lower anytime soon. Instead, a reversion to the 4-6% level is my base case, which compares with Fed Funds rate expectations of about 5%, a level that would merely compensate for the loss of purchasing power, and thus can be considered neutral at best. The situation is even worse in Europe, where inflationary pressures especially from the energy side and due to a weak EUR are much higher, while the ECB is not hiking as determinately as the US Fed.

And yet, investors are still betting on a central bank monetary policy pivot, which is generally described as a shift from contractionary to expansionary policy (or vice versa). After all, this has been the MO in recent years: Tightening monetary policy until something is at risk of breaking, followed by a policy pivot. But especially the Fed, but also other central banks, are now telling us that they may simply pause hiking rates at some point, rather than revert to a new cycle of interest rate cuts.

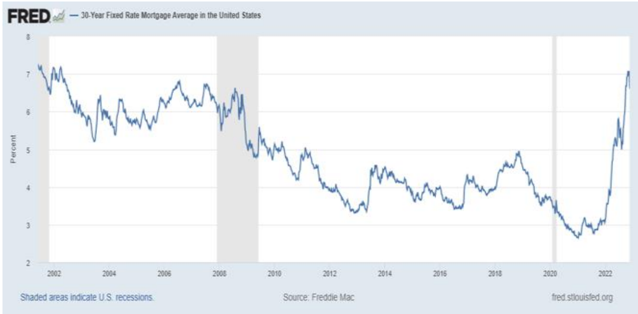
Personally, I don't doubt that this is what they will attempt to do. But if the past has taught us anything, then it is that the measure of control that central banks (as much as other political players) have about the complex system we generally call economy, is lower than they believe. Because the cocktail of elevated nominal rates in our highly leveraged economies, mixed with a sharply slowing economic growth rate, is a perfect recipe for something serious to break. And I doubt that such a scenario has been priced in by investors…

In this regard, we do not have to look merely at financial markets. Taking the housing market, it is obvious how the extended period of zero (or even negative) interest rates has lifted house prices far beyond the growth rate in incomes. This in turn has led to a collapse in affordability, as measured by sharply rising house price-to-income ratios across the world.

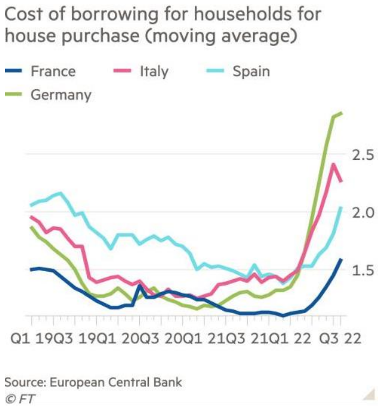


@RichardDias_CFA, Twitter, 11OCT2022

The growing lack of affordability is further boosted by rising borrowing cost. The graph on the right shows US 30y fixed mortgage rates, which have gone from as low as 2.8% in early 2021 to nearly 7% by now. Arguably, the prevalence of this financing type insulates existing borrowers from rising rates, but for new buyers it adds to the affordability challenge.



30-Year Fixed Rate Mortgage Average, FRED - St. Louis Fed



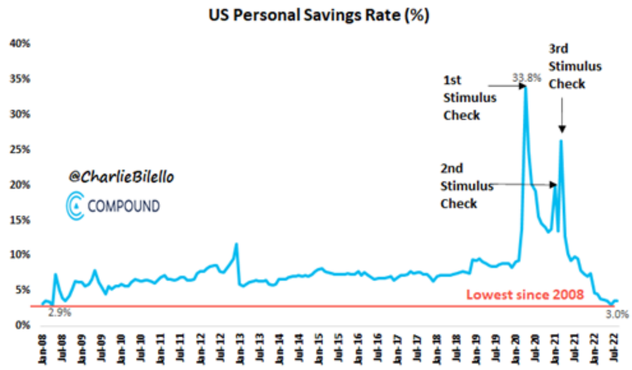
Financial Times, 3NOV2022

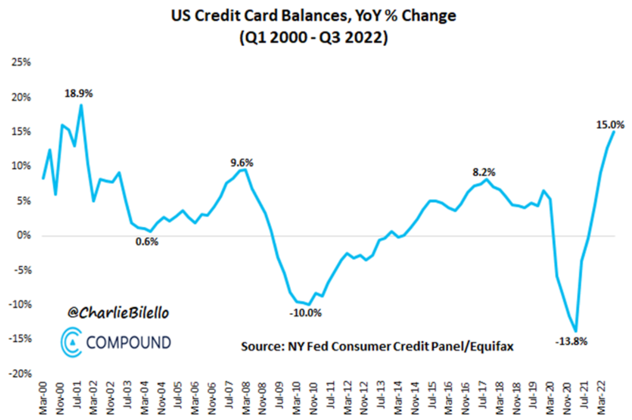
The situation is similar in Europe, where mortgage rates are also climbing, though from a much lower level. On the continent, longer-term financing arrangements tend to prevail which to some degree insulates borrowers from sudden rate increases. UK real estate owners are expected to suffer the most, as UK mortgage loans have predominantly variable rates, which even for existing owners does immediately hike housing cost. But whether the adjustment is short- or more medium- to long-term, it is evident that money spent on mortgage loans is unavailable for other expenditure.

When we consider housing cost or food or energy, these are categories that economists' group under non-discretionary spending. Sure, we can save on food cost by changing our diet or food quality, but we must still eat. Equally, we must service our mortgages or pay rent, to avoid foreclosure or risk of eviction.

Since nominal incomes are rising more slowly than inflation, this means cutting back on discretionary spending. – Do we really need Netflix, Disney+, Hulu, Sky, or any of the other numerous streaming services, or does one not suffice? – Do we have to dine out that much, or instead rather eat at home? – Do we really need more new cloths or a vacation, or that new TV set, smartphone, or car, if the old one still works fine?

Households can cushion the blow to their purchasing power by tapping into savings or even running up credit card debt, which is already happening as illustrated by the two charts on the right, courtesy of Charlie Bilello at compoundadvisors.com. But a more sustainable way to address the experienced loss of purchasing power is to demand higher wages and employment compensation. This leads to the dreaded wage-price-spiral, that central banks aim to prevent by keeping interest rates higher for longer, with the implicit goal to reduce overall demand sufficiently to ease prevailing pricing pressures. And this in turn yields exactly the stagflationary (i.e., economic **stag**nation coupled with price in**flation**) scenario, I have been writing about in recent issues of Seasonal Reflections.





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I guess I could go on like this but definitely don't want this to sound too gloomy. In the end, and as always, our changed circumstances require an adjustment process that has already begun and is unlikely to reverse, and I am optimistic that mankind will make the best of it. But I also have no doubt that it will lead to some serious belt-tightening and a longer period of subpar to negative real economic growth. And it is equally likely to cause a wealth distribution shift in advanced economies from favouring capital and its owners to labour, which in my view will make the coming decade in financial markets far more challenging for investors than the past.

This is why, given our highly leveraged economies and financial system, I find it incredible how sanguine investors are concerning rising interest rates. The past impact of low, zero or even negative rates on financial asset valuations simply cannot be underestimated. As Michael Lewitt in his Credit Strategist Blog recently stated:
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"Low rates lowered IQs along with the value of the financial instruments they debauched, leading people to buy worthless SPACS and cryptocurrencies, grossly overvalued IPOs, even more grossly overvalued stocks after they went public, and egregiously overvalued credit instruments of all kinds. Now the cost of money is being reset by central banks because they lost control of the inflation narrative (they lost control of inflation – particularly financial asset inflation - long ago).

Investors have yet to adjust to the cost of money which is not going back to zero (or below zero) absent another financial crisis (which if you look at government finances is a real possibility, but that is a topic for another day). For now, rates will remain well above zero and that means all the assumptions that led public and private actors to borrow trillions of dollars are going to be tested (and borrowers will flunk those tests)."

Warren Buffett in his wisdom and wit has famously framed this as follows: *"Only when the tide goes out do you discover who's been swimming naked."* - The crash in non-profitable tech stocks, as illustrated by the round-trip Cathy Wood's ARK Innovation ETF investors had to endure, the collapse in high-flying meme-stocks, or the recent turmoil in crypto-land all show that this quote is as true as it ever was.

ARK Innovation ETF, NYSE, investing.com

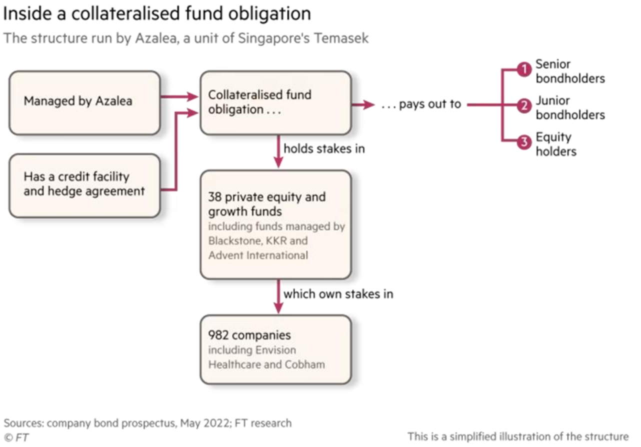
This has been the result of USD 30 trillion of QE (= Quantitative Easing, which is the label for central bank (financial) "asset" purchase programs, where the "assets" in question were mostly bonds, which are in fact liabilities): Low risk "assets" were bought by global central banks irrespective of price and yield, leaving the seller of these bonds with freshly minted cash to deploy in more high-octane investments that at least promise a real return, at surely manageable risks. - And what has that led to?

Bloomberg, 14OCT2022

Well, take a look at the graph on the left, dear reader. It shows the allocation to alternative assets (mostly private equity & credit, hedge funds, etc) by the world's largest investors, i.e., all sovereign wealth and pension funds. These are considered very sophisticated investors, who employ scores of financial experts and managers in their selection and allocation teams, and all of them have increased their allocation to alternative assets, some like Canada's CPPIB to the tune of 50%.

And now that the tide is going out, the true degree of indecency is gradually revealed. Just looking at the list of major investment firms that had backed recently imploded crypto empire FTX indicates the true state of affairs (for more details see this NYT article). If the likes of Tiger Global, Sequoia Capital, SoftBank, Temasek Holdings, BlackRock or Thoma Bravo, with their hundreds of billions in AuM all did proper due diligence on their investments, how could they not get suspicious but instead lose hundreds of millions of their beneficiaries' moneys?

And how does the industry – hardly unpredictably – respond? – Following the Great Financial Crisis playbook, the shoe that is yet to drop is revelation of losses in the Private Equity / Credit sphere. And thus, a recent FT article titled "How private equity securitised itself", may be a harbinger of sorts. It describes how the industry is making a big push to bundle up PE funds in so-called CFO (Collateralized Fund Obligations), which are *"in some ways, a private equity variant of* "collateralised debt obligations", *the bundles of mortgage-backed securities that only reached the public consciousness when they wreaked havoc during the 2008 financial crisis."* (Financial Times, 25NOV2022)



Financial Times, 25NOV2022

The article about what an industry insider has labelled *"the technicolour dreamcoat of fund finance"* continues: *"CFOs introduce a new layer of leverage into a private capital industry already built on debt."* It is essentially a collection of PE funds, securitized and sliced into different tranches of seniority with regard to their claim on cash flows from the underlying investments, essentially like their predecessors helping to turn sh.. into gold, as the most senior tranches unsurprisingly have been receiving A-ratings.

For Private Equity groups it is just another way to get rid of risks on their balance sheets and raise fresh funds. After all, as the report continues: *"the conditions that fuelled private equity's boom have gone into reverse. Buyout funds have been on a dealmaking spree for several years, buying record numbers of companies at eye-watering valuations, some of which are now facing an uncertain future as an economic downturn kicks in and borrowing costs rise."* – Enough of a reason to lighten up, I guess.

And unsurprising, *"So far, CFOs have escaped much regulatory scrutiny, in part because they are private offerings which require little in terms of public filings."* – Well, my doubts about the quality and thoroughness of investors due diligence are probably unsurprising… – And after this one blows up, we will get another round of hard-core regulation that comes far too late for the true culprits, but will make life for your plain vanilla asset manager more difficult and expensive… – Nothing new in the investing business…

The undisputed fact is that every period of excessively easy money has bred this kind of behaviour, when investments are made on their relative merit, underpinned by rosy outlooks, while holding one's nose over the potential risk.

This is the environment that free money has created, and the trouble is, it is no longer free!

Chart 7 Long term charts of tech...
Tech vs S&P 500 price relative

Source: BofA Global Investment Strategy, Bloomberg, Global Financial Data
BofA GLOBAL RESEARCH

The Macro Tourist Private Twitter Feed Recap, 20OCT2022

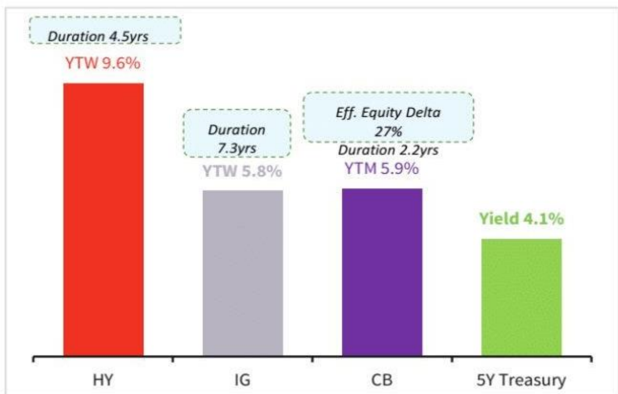
In this respect, it is also important to note that TINA (**T**here **I**s **N**o **A**lternative (to equity and alternative investments) has been suspended from service until further notice. As the graph on the right shows, for the first time in what seems like eternity, bonds offer a credible and lower risk liquid yield alternative to investors, and I believe this – as much as expectations of slowing inflation pressures – has led to the recent consolidation in yield levels (5-year Treasury yields have fallen 15bp to 3.95% at the time of me penning these lines).

Source: Hedgeye

But, I hear you say, could the worst not be behind us already?

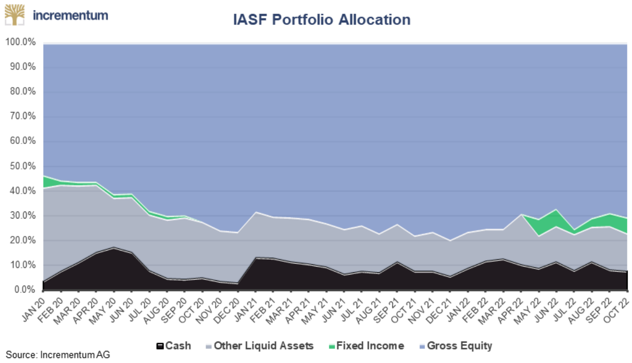
Sure, anything is possible, as a lot of things have happened in this cycle that I would never have thought possible. But I don't think it is likely, and I would certainly not want to bet my own or my investors' hard-earned money on such an outcome. Instead, my central thesis that we are still in the process of the evolving rotation out of tech / growth / non-necessities into hard asset / value / essentials continues to dominate **IASF's** investment allocation and portfolio positioning.

FIGURE 12. **There are credible alternatives to equities**



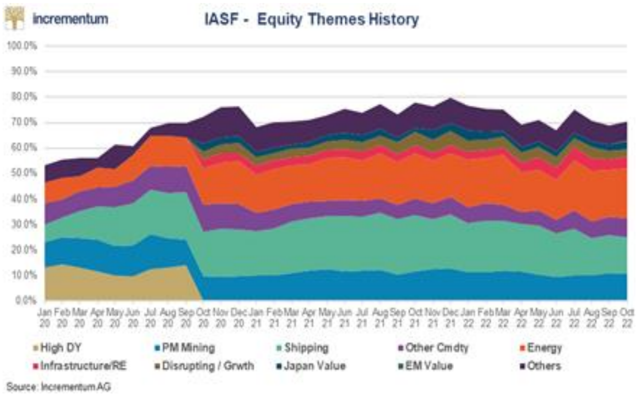
YTM for CB is defined as Max(CY, YTP, YTM). Values as of 10/12/2022
Source: Bloomberg, Barclays Research

M'tourist Private Twitter Feed Recap, 19OCT2022

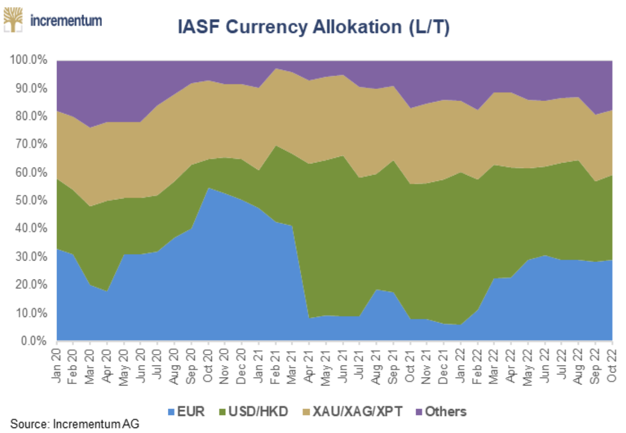


Consequently, **IASF** has begun building a still relatively small bond position, with attractive yield levels that we think will exceed inflation rates over the coming few years. However, the bulk of our portfolio allocation (approx. two thirds) continues to be equities, and here still in themes and individual picks that we believe offer attractive value.

Our thematic equity basket is currently dominated by ENERGY and SHIPPING, which are both supported by medium-term macro tailwinds, but have seen their overall allocation reduced amid profit-taking. PM MINING has been a constant part of the allocation, given our medium-term bullish outlook for precious metals prices, which in turn are the most important driver for stock prices in this sector.

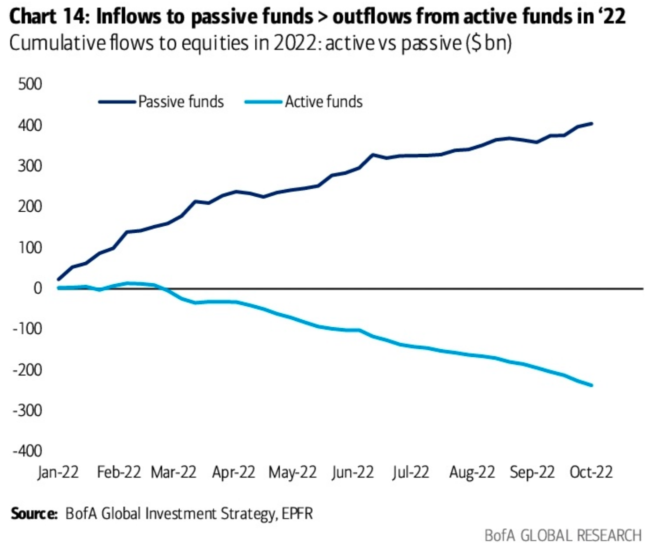


OTHER COMMODITIES has been fairly steady and covers mostly diversified plays, with an emphasis on copper, as well as fertilizer producers. OTHERS is a ragbag of bottom-up stock picks, which do not easily fit into the major theme baskets, but offer what we look for in equities, namely decent value and thus appreciation potential on top of any cash flows shared with investors through dividends and buybacks. INFRASTRUCTURE / REAL ESTATE has by now also exceeded the 5% allocation level.



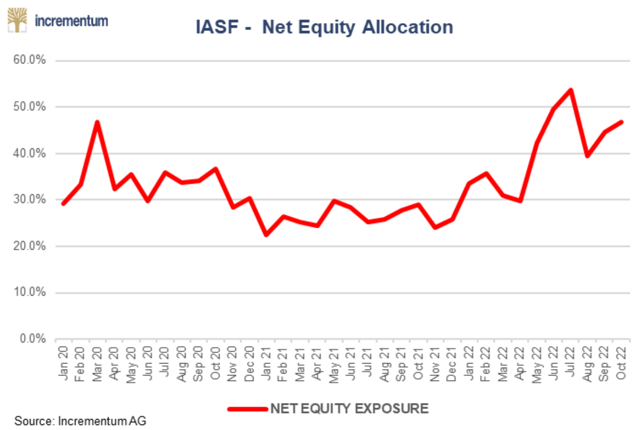
PM MINERS play a special role, not only because they have rarely been as cheap as they have recently been, but also because they help us diversifying our currency allocation. And as we expect precious metals to gain in value versus fiat currencies over the coming years, we include precious metals miners in our XAU/XAG/XPT (Gold/Silver/Platinum) exposure, which as the chart shows has also been a fairly constant fixture in our overall FX allocation.

We still work in a world that is dominated by passive investing, as the graph on the right obviously proves. Here, we clearly want to make a difference.



@DylanLeClair_, Twitter, 8OCT2022

What characterizes our active investment approach? – Among others, the fact that we don't use index funds in our asset allocation, or that our equity allocation is as far away from any of the major stock indices as one could imagine, or that we actively manager our foreign currency exposure through currency overlays, or just by well over 800 individual transactions registered so far this year.



Another indicator for our active management is our net equity allocation, which has been fluctuating between 20% and 60%, mainly driven by the opportunities we found in going long equities, and the degree we felt it sensible to hedge our long exposure via short equity index future positions. But this again is no permanent fixture, and we hope that soon we can unwind all our hedges as we already did once for a few weeks in March 2020.

And lastly, we have been actively harvesting risk premia by selling options against cash or existing fund holdings, which has been a great way to enhance our income from the overall investment portfolio, contributing nearly 7% to this year's overall performance (year-to-October 2022), while we rarely had more than 10% of underlying assets at risk. The active covered option writing strategy is also the main reason for the large number of individual transactions recorded so far this year, as we have often used this tool to rebalance existing portfolio holdings.

What are our challenges at the end of November, when I am furiously typing to try and finish this piece? To determine

- whether the bear market in equities is over (we reckon it is not),
- whether the USD has turned the corner and will enter a longer-term bear market from here (we reckon it will not (yet)),

- and most importantly, whether our current investment themes still provide sufficient tailwinds to justify current allocations, and how we can populate the newer and smaller ones with value accretive picks.

I hope that this latter part of the report has helped investors to better understand how this year's extraordinary results were achieved, which I fear will be next to impossible to repeat – though we will certainly try. And please remember with everything I have commented on in this report:

THIS IS NOT INVESTMENT ADVICE!

As author of this newsletter and responsible fund manager of the Incrementum All Seasons Fund, I must remind readers that all views expressed in this report, especially those concerning the fund's individual investments or investment strategy, are biased, and not tailored to their individual needs. And although I write this commentary with care, I cannot vouch for the accuracy of any statement made herein. Seasonal Reflections are issued to registered subscribers for information and entertainment purposes only and must neither be seen as an attempt to solicit an investment in individual securities nor in the Incrementum All Seasons Fund. Hence, if you are looking for investment ideas or advice, always consult a licensed investment professional! And remember that past performance is no guarantee for future returns and that all investments involve risk, including loss of principal.

Ok, with this out of the way, allow me to bring an interview to your attention, which Stanley Druckenmiller gave to CNBC on 28th of September 2022, under the title *"Navigating The Market with the World's Top Investors"*, which I believe is worth watching.

And with that I would like to close this issue of my Seasonal Reflections. As always, I welcome readers' feedback by e-mail, and sincerely thank you all for your interest and our investors for their trust and support. And considering the season, **I would like to wish you a wonderful pre-Christmas season, happy holidays, and a great start into 2023!**

Greetings from Schaan, Liechtenstein!

Best regards,
Hans

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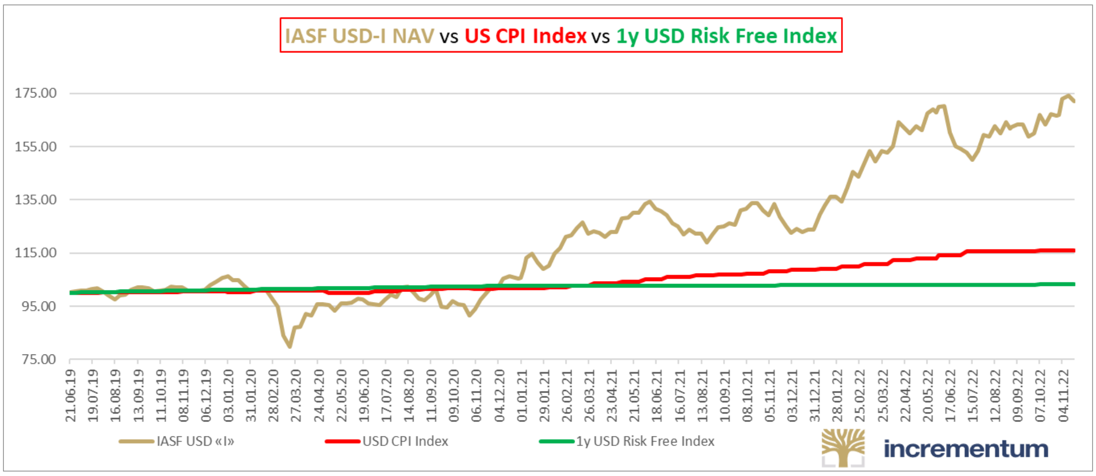
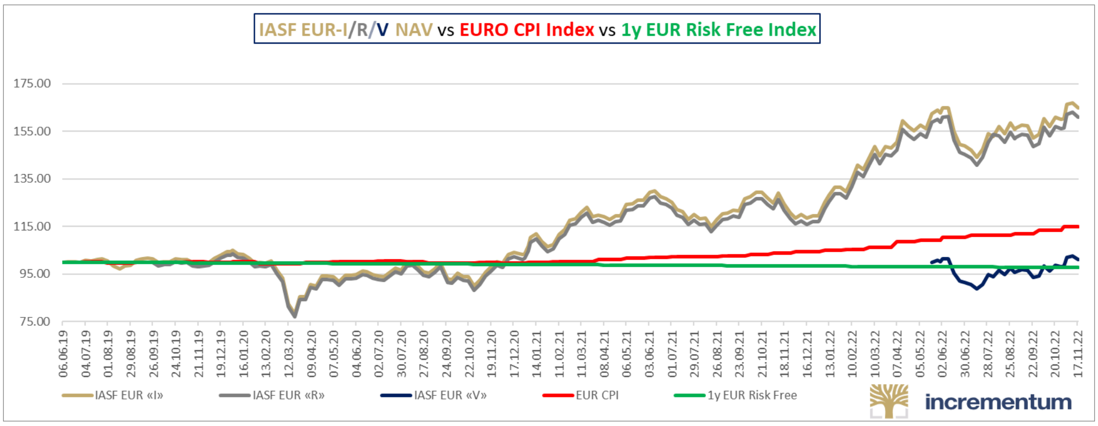
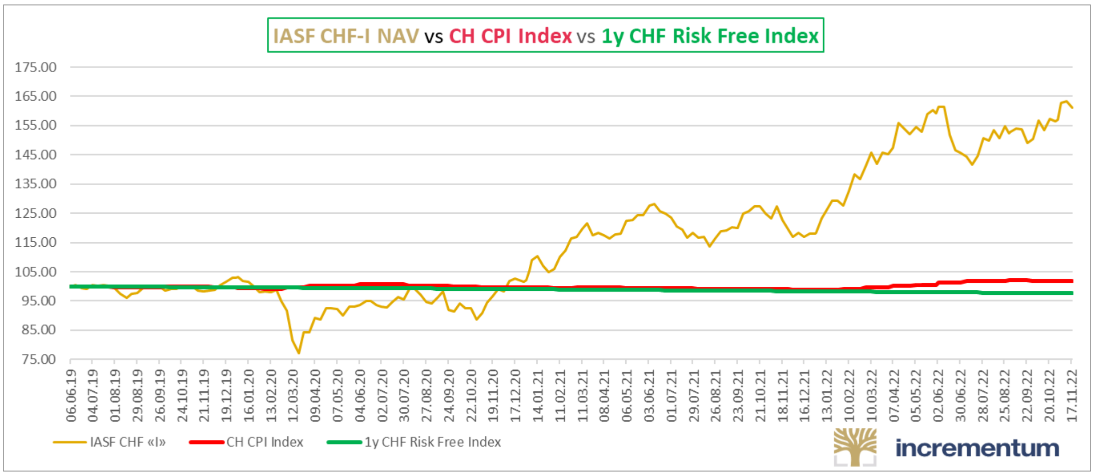
Appendix *







* Graphs display NAV of IASF performance until last valuation date (**31AUG2022**), compared to the respective risk-free 1y-government yield, as well as the relevant CPI Index in respective currency as a proxy for the loss of purchasing power from the start of the investment period (6Jun2019 for 'I' shares; 26Sep2019 for EUR-R shares; 20MAY2022 for EUR-V shares) 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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