Q3 General Update

OCTOBER 2022

We build and maintain portfolios for clients which address their specific needs

Baggot is a Central bank regulated investment manager. We specialize in designing and monitoring investment strategies that are built using global investment products and assets. Where almost all financial advisors and brokers would simply refer your business to a large external manager, in return for a commission, we use in-house expertise to actively manage your assets.

We offer Investment strategies across various risk profiles. In many cases, we build portfolios in-line with our client's specific needs (CGT focus, Income focus, etc.).

As a principle at Baggot, we do not charge upfront fees or expose our clients to lock-up periods. You can add or withdraw funds at any time and switch between strategies at no extra cost.

If you would like a review of your current investment strategy or to discuss future investment opportunities please contact us.

Call 01-699 1590

Peter Brown
Managing Director

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Before getting into product returns it should be noted that our product return numbers include all charges, which is not the case for our peers

01.

Baggot returns summary

BEI, our global equity income focused product (medium-high risk profile) has outperformed the benchmark Setanta Equity Dividend Fund by 13.2% through Q3 of this year. The benchmark lost – 10.3% in the first 9 months of the year while BEI has gained 2.9% for the same period. It has been a good start to Q4... As of today BEI has gained 6.95% YTD.

BME, our higher risk profile product outperformed the benchmark MSCI World Index by 15.9% through Q3 of this year. The benchmark MSCI World index posted a loss of - 13.25% during the period, while BME has posted a gain of 2.65% for the same period. It has been a good start to Q4...As of today BME has gained 5.45% YTD.

BMA 4, our medium risk multi-asset product has outperformed the benchmark Irish Life MAPS 4 by 5.2% through the first three quarters of this year. The benchmark Irish Life MAPS 4 lost – 11.8% for the same period. The benchmark lost – 11.8% in the first 9 months of the year while BMA 4 lost – 6.6% for the same period. It has been a good start to Q4...As of today BMA 4 is down -3.8% YTD.

BMA 5, our multi-asset product with a medium-high risk profile has outperformed the benchmark Irish Life MAPS 5 by 6.8% so far this year. The benchmark Irish Life MAPS 5 lost – 14.4% through Q3 of this year. BMA 5 posted a – 7.55% return for the same period. BMA 5 has started Q4 out well with a 2.4% gain, narrowing the YTD loss to – 5.15%.

Before I move on, I'd just mention that the four products mentioned would be our more popular products but we do have other investment products that have been tailored more to the specific needs of some clients which have all posted very competitive returns.

For any further information contact pbrown@baggot.ie.

02.

Market returns summary

Asset class return numbers noted below are all based in Euro denominated terms. Data taken from unhedged (currency) European UCITs ETFs, which include costs as well as dividend payments.

For perspective when comparing returns, the EURUSD lost – 6.03% in value in Q3, not including "carry" which is the difference in yield between the Euro and US Dollar. In total you are looking at a roughly - 6.7% loss in value in Q3 for EURUSD.

Q3/YTD Equity Returns (Euro denominated returns)

S&P 500
1.4% / -11.7%

NASDAQ 100
1.7% / -21.6%

Euro Stoxx
-3.7% / -20.8%

German DAX
-5.3% / -24.1%

Stoxx Europe 600
-5.9% / -17.8%

FTSE 100
-5.5% / -8.4%

MSCI EM Asia
-8.4% / -16.2%

Vanguard FTSE EM
-4.6% / -11.5%

MSCI China
-17.5% / -20.3%

MSCI Japan
-1.7% / -14.8%

MSCI Word
-0.1% / -13.5%

MSCI Latin America
9.5% / 18.4%

MSCI India
13.5% / 4.5%

MSCI Asia Pacific ex-Japan
-7.0% / -15.0%

Q3/YTD Bond returns (Euro denominated returns):

Europe Investment Grade Ultrashort dated
-0.3% / -0.09%

German 10+ Year Bond ETF
-8.1% / -29.2%

US 10+ Treasury Bond ETF
-3.7% /-17.4%

Europe Aggregate Bond ETF
-4.6% / -16.3%

EM Bond ETF
1.2% / -12.5%

Global Aggregate Bond ETF
-0.9% / -7.1%

US Inflation Protected Bonds
0.9% / -0.2%

Europe Inflation Linked Bonds
-5.1% / -11.0%

Q3/YTD Precious metals (Euro denominated returns):

Gold
-2.8% / 5.3%

Silver
-3.2% /-6.0%

Q3 Asset Class Returns Summary

An exceptionally difficult time for most assets with correlations uncomfortably high across asset classes for much of the quarter.

Equities

In Equities the big losers in Q3 were the MSCI China with a – 17.5% return, the MSCI EM Asia with a – 8.4% return and the MSCI Asia Pacific ex-Japan posted a return of – 7%.

The winners in Q3 were the MSCI Latin America with a 9.5% gain and the MSCI India with a 13.5% gain.

Bonds

In Bond land, German 10+ Year Bunds once again had the worst showing, down – 8.1% in Q3, followed by European Inflation Linked Bonds which lost – 5.1% and European Aggregate Bonds, down – 4.6%.

The relative winners were US Inflation Protected Bonds which gained 0.9% in Q3 followed EM Bonds which gained 1.2% and Europe Investment Grade Ultrashort dated Bonds which lost – 0.3% for the quarter.

Precious Metals

Gold gave up – 2.8% on the quarter but on the year it continues to demonstrate its importance as a safe haven....Year-to-date, Gold is still up 5.3%. Silver posted a return of – 3.2% in Q3. Year-to-date, Silver is down – 6% which is nothing to shout about but you could do a lot worse this year in many other assets with the same risk profile.

03.
Bonds

Where we must have bond exposure (due to risk constraints) we continue to keep pretty much all of our exposure in ultra-short dated European investment grade bonds - which carry the lowest risk profile possible. If we had a choice we wouldn't hold any bonds whatsoever, but among multi-asset portfolios when you own higher risk profile assets such as equities and commodities, then in lower to medium risk profile investment products, you must offset that risk with something that has a very low risk profile.

We would much prefer to own longer duration bonds to the ultra-short, dated ones because yields are better in longer duration but as I have said all year, we think that is about as wise as trying to pick up a nickel in front of a steam roller. The gap between inflation and interest rates is very wide. At the moment inflation is still running at 8.3% in the US with three month interest rates in the US trading at 3.4% and in Europe inflation is running at 8% with three month interest rates at 0.75%. The gap between inflation and yields is just too wide to change our stance. This creates a lot of risk for longer duration bond investors.

Our bond stance has not been exciting but when you consider that the German 10+ Year Bond (Bund) ETF has lost – 29.2% YTD and the US 10 Year+ Treasury Bond ETF has lost – 17.4% YTD while our position is pretty much flat for the year, we're obviously quite happy with that. It's no fun sitting in ultra-short duration investment grade bonds when yields are so low, but even if inflation comes down to half the current rate of inflation, interest rates must surely go dramatically higher and that means the selloff in long and medium duration bonds is nowhere near finished.

Ideally, you'd like to see 3% inflation and 5% yields. That is a 2% positive real rate (the difference between inflation and interest rates). Currently even in the US you are looking at – 4.9% negative real rates and Europe is more like – 7.1% negative real rates. We still feel that we are a long way from being able to confidently hold long duration government bonds again. Long duration government bonds represent 'return free risk' as opposed to a 'risk free return'.

Yields in Emerging Markets are much more attractive but a lot of debt in Emerging Markets is priced in US Dollars, so as the Dollar goes higher (as it is now) the liability grows for Emerging Market bond issuers. At some point when the Dollar starts to weaken against Emerging market currencies, yields in Emerging Markets are going to be quite attractive, so that is an area we are watching closely for opportunity but it could be a while.

04.

Equities

In our last two General Updates I have suggested that the inflationary impact of the war would likely hit corporate profit margins and that we see a very high likelihood of lower growth and higher inflation (Stagflation) going forward. We continue to have strong conviction in that outlook.

I posted this last Qtr and it is still very relevant. Look at sector performance during periods of stagflation. We've highlighted real returns (return after taking account of inflation).

Start	End	Materials	Discretionary	Industrials	Energy	Health Care	Financials	Staples	Info. Tech.	Telecom	Utilities
Q4/1973	Q3/1975	18.9%	-7.9%	-13.6%	-4.0%	-11.0%	-21.0%	-10.0%	-24.3%	-2.6%	-11.1%
Q2/1979	Q2/1981	26.6%	17.0%	33.2%	54.2%	29.3%	37.4%	20.4%	-7.9%	-5.8%	-4.4%
Q1/1982	Q1/1983	48.5%	70.5%	55.2%	17.8%	43.0%	41.2%	45.8%	79.3%	15.9%	16.8%
Average Nominal Return		**31.4%**	**26.5%**	**25.0%**	**22.7%**	**20.4%**	**19.2%**	**18.7%**	**15.7%**	**2.5%**	**0.4%**
Average Real Return		**17.6%**	**12.7%**	**11.1%**	**8.9%**	**6.6%**	**5.4%**	**4.9%**	**1.9%**	**-11.3%**	**-13.4%**

Source: Bloomberg, Incrementum AG

We continue to favour Value focused Equities over Growth. In the West, we think you have to avoid the big US indices because so much of the risk exposure in those indices is in areas that to us look like a fly in search of a windshield. That is not to say that there are not Sectors or Industry Groups that we have a favourable view of in the US, such as Energy and Materials but those Sectors are a very small proportion of the Index as a whole..

We try our best to align good valuations with strong relative performance. From that perspective we are really impressed with how well Latin American Equities and also Indian Equities have performed this year. India on the surface does not look cheap, but relative to its growth rate it is quite attractive. We're also impressed with how well some of the more commodity-centric equities have acted in spite of the strong Dollar.

If they can perform like this, in this environment, imagine how well they will do when the Dollar begins to weaken!

We're currently more focused on Emerging Markets and Natural Resources Equities but within Developed Markets we favour the FTSE 100 and Japan as there is a strong combination of currency debasement (export competitiveness) and relatively cheap valuations.

Valuations below taken from Reuters. I've highlighted relatively cheap areas in green and relatively expensive areas in red;
P/E = Price/Earnings Ratio, P/B = Price/Book Value Ratio

- Nikkei 225 (Japan): P/E of 12.9 and P/B of 1.0
- Nasdaq 100: P/E of 25.1 and P/B of 6.2
- S&P 500: P/E of 20.0 and P/B of 3.2
- FTSE 100: P/E of 12.1 and P/B of 1.8
- CAC 40: P/E of 15.5 and P/B of 1.4
- German DAX: P/E of 15.3 and P/B of 1.8
- FTSE Eurofirst 300: P/E of 15.1 and P/B of 2.0
- S&P TSX (Canada): P/E of 14.9 and P/B of 1.7
- S&P ASX 300 (Australia): P/E of 14.7 and P/B of 1.8

Remember, the FTSE 100 is much more an international index than it is a UK focused index, but with the kicker of a weak currency which makes those international companies more competitive.

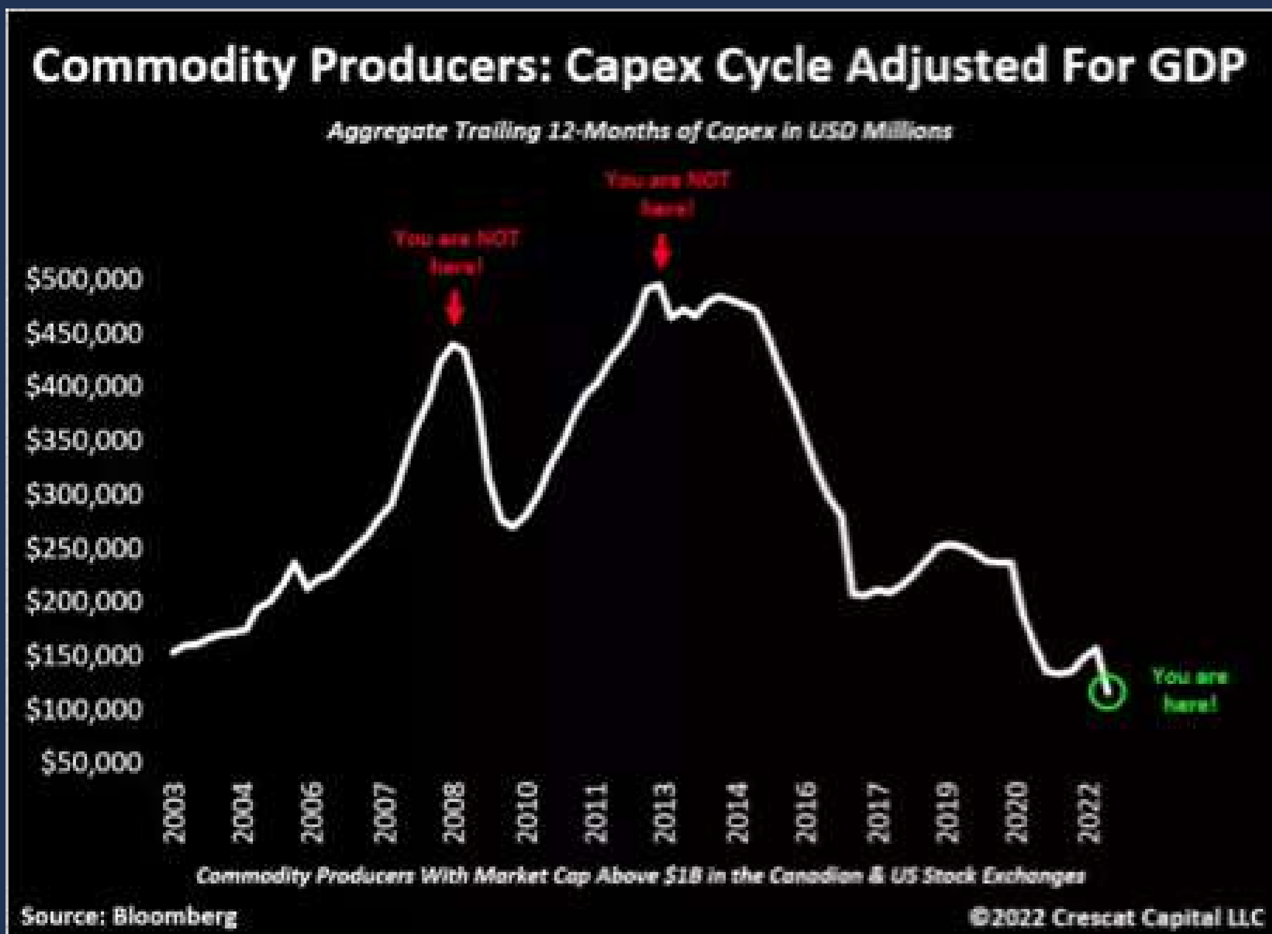
We do see more potential in Commodity-centric Equities than we do in your standard plain vanilla indices. Commodities are still ridiculously cheap relative to Equities. We'll dig a little deeper on the Commodity front below.

05.

Commodities

We have seen some pullback in most major commodities over the last few months. We believe the pullback has created an excellent long term buying opportunity. We do believe there will be some demand destruction in commodity land brought on by tighter central bank monetary policies, but central bank policies have no impact on the supply side. When you look at the supply side of things across many different commodities, structural supply deficits suggest that we will need to see significantly higher prices in order to bring enough supply to the market to satiate demand.

"The Fed is determined to cause a recession to control the demand side of inflationary pressures. By its own admission, the central bank can do nothing to solve the supply-side of the inflationary problem today. As economic Nobel Prize winner Joseph Stiglitz recently advised, the Fed's recent actions are only likely to make supply-side inflationary pressures worse. At Crescat, we have been highlighting the truly unprecedented structural shortages for natural resources which are best illustrated by looking at aggregate CAPEX spending trends for commodity producers. While many investors are selling commodity stocks because they fear it will be another 2008-style deflationary global financial crisis or 2015-style commodity bust, we show below that it is exactly the opposite setup now."
– Tavi Costa of Crescat Capital (A highly respected global macro hedge fund)



“Metals of all varieties are critical to inflation protection, economic growth, and energy transition in the real world today. These are the factors that matter in the current macro environment. The companies that control the best new metals’ deposits, offer deep value, strong growth, and ultra-high appreciation potential in the stock market now.” – Tavi Costa of Crescat Capital (A highly respected global macro hedge fund)

Now consider how utterly cheap commodities are relative to equities from a longer term perspective. The chart below shows the S&P GSCI (Goldman Sachs Commodity Index) Total Return Index Divided by the S&P 500 over the last 5 decades. If it is rising it means commodities are outperforming equities. If it is falling it means equities are outperforming commodities. When the graph is closer to the bottom of the chart window, it means commodities are exceptionally cheap vs equities. When the graph is closer to the top of the chart window, it means equities are exceptionally cheap vs commodities.

Not only are we looking at structural supply deficits for most commodities, we are also being given the opportunity to own many of these commodities and commodity companies at ridiculously cheap prices relative to the main equity indices.

You can have commodity companies that supply many of the materials needed to fuel the green revolution with low debt levels, decent balance sheets and high free cash flows...things the world actually needs, or you can have the big western equity indices generating negative real free cash flow (free cash flow after taking account of inflation).

Tech Stocks: Real Free-Cash-Flow Yield
Aggregate Free-Cash-Flow Yield Minus CPI YoY Change
10.00
8.00
6.00
4.00
2.00
0.00
-2.00
-2.8727
-4.00
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024
Source: Bloomberg
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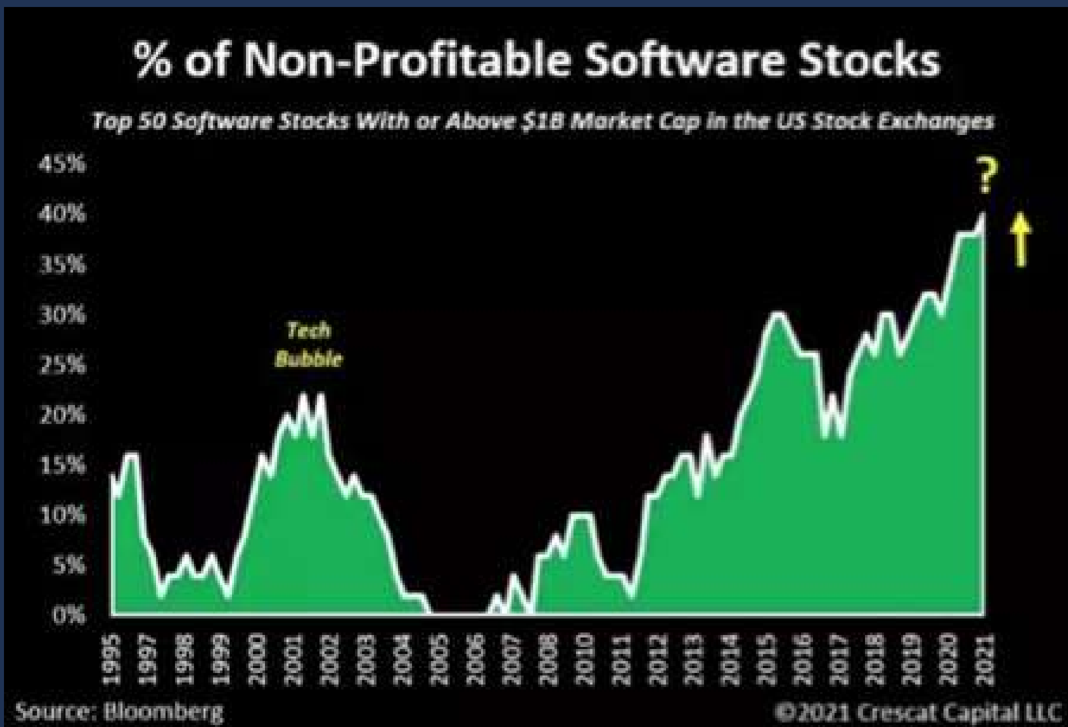
% of Non-Profitable Software Stocks
Top 50 Software Stocks With or Above $1B Market Cap in the US Stock Exchanges
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
Tech
Bubble
?
1995
1997
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
Source: Bloomberg
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China (responsible for almost half of global commodity consumption) is coming out of a long lockdown period which has certainly cut global demand for energy to some degree. Add to that the fact that the Biden Administration has been releasing 1 million barrels per day (bpd) from the Strategic Petroleum Reserve (SPR) which has also been an impediment to higher Crude Oil prices. This cannot go on forever until these reserves are depleted. The SPR is already at dangerously low levels.

We believe the Biden administration have most likely timed these SPR releases to drive oil prices lower into mid-term elections to try and buy votes for the Democrats. We don't see how the SPR can continue down this path after the mid-term elections (November 8). In fact we expect that the administration will have to reverse course after and begin to buy oil to bring the SPR back to more reasonable levels.

Add in the fact that OPEC and allies, including Russia have just agreed to slash oil production by 2 million barrels per day and we are looking at a much tighter oil market for the remainder of the year.

Bring China back to normal consumption post-lockdowns and discount an end to the SPR releases and my belief is that you have more than offset the weaker demand that has been brought about by tightening monetary policies. We see risk to the upside for Crude Oil and Natural Gas prices. Given that energy is directly and indirectly a huge component of the inflation data, if prices do head higher over the coming months, we would expect central banks to become even more hawkish.

06.
Uranium

Uranium has been one of the better performing assets in our portfolios this year. As I write this letter, it is up about 27% YTD in Euro denominated terms. The long term investment case hasn't changed. Nuclear is the only scale-able zero emissions bridge to a carbon free world. It is also an easy way to remove energy dependence on countries that do not have our best interests at heart. Because of Fukushima it went through a long period of underinvestment. Consequently there's nowhere near enough supply relative to demand and nuclear power generation continues to grow.

In the last quarter we've seen some pretty dramatic political shifts in favour of nuclear. See the below headline and link.

Post-Fukushima Shift: Political and Public Support Rises in Japan for More Nuclear Plants;
https://www.zerohedge.com/commodities/post-fukushima-shift-political-and-public-support-rises-japan-more-nuclear-plants

Even Germany seems to be moving more in the direction of a nuclear renaissance which makes sense when you consider that they can either embrace it or continue importing coal and Russian Gas.

There are 220 new nuclear power plants planned in Asia;
https://www.weforum.org/agenda/2022/01/asia-nuclear-reactors-power-energy/

Even Poland is getting in on the act;
https://www.power-technology.com/news/bechtel-nuclear-power-poland/

Where will all the Uranium come from?
Currently prices are trading around $48 - $49 per pound. We believe prices could reach $60 per pound in the next 3 – 6 months and we see the potential for $100 per pound in the next 24 months. We continue to be very bullish on Uranium prices from a long term perspective and see it as an important inflation hedge.

Near term you must consider that it has always been a volatile risk asset and that it does face the headwind that all risk assets face at this time. The Fed and other central banks are removing liquidity from the system via interest rate hikes and balance sheet reduction. This leads to forced liquidation across assets and for shorter term periods that can cause correlations to rise across the board making most riskier assets behave the same way at the same time. As long as that is the case there is certainly some near term downside risk, but the bottom line is this; there's a primary deficit in this market. Nuclear power plants operate on long term contracts, many of which are rolling off this year, and they have to procure supply for the future and will be renegotiating at significantly higher prices. Ultimately if you want a zero emissions world and you don't want people in the developing world to starve or freeze to death, Nuclear is the only scale-able, viable way to do it.

MEASURING RADIATION EXPOSURE

Radiation stemming from nuclear energy is far less when compared to activities not commonly associated with nuclear activities, such as flying on an airplane or interacting with more traditional energy sources.

MILLIREMS OF RADIATION (MREM)

5,000	Annual U.S. regulatory radiation limit for an adult
500	One transcontinental round trip flight
360	Average person's annual exposure from all sources
20	Living one year outside a coal plant
2	Living one year outside a nuclear power plant

Source: U_3O_8 Corporation.

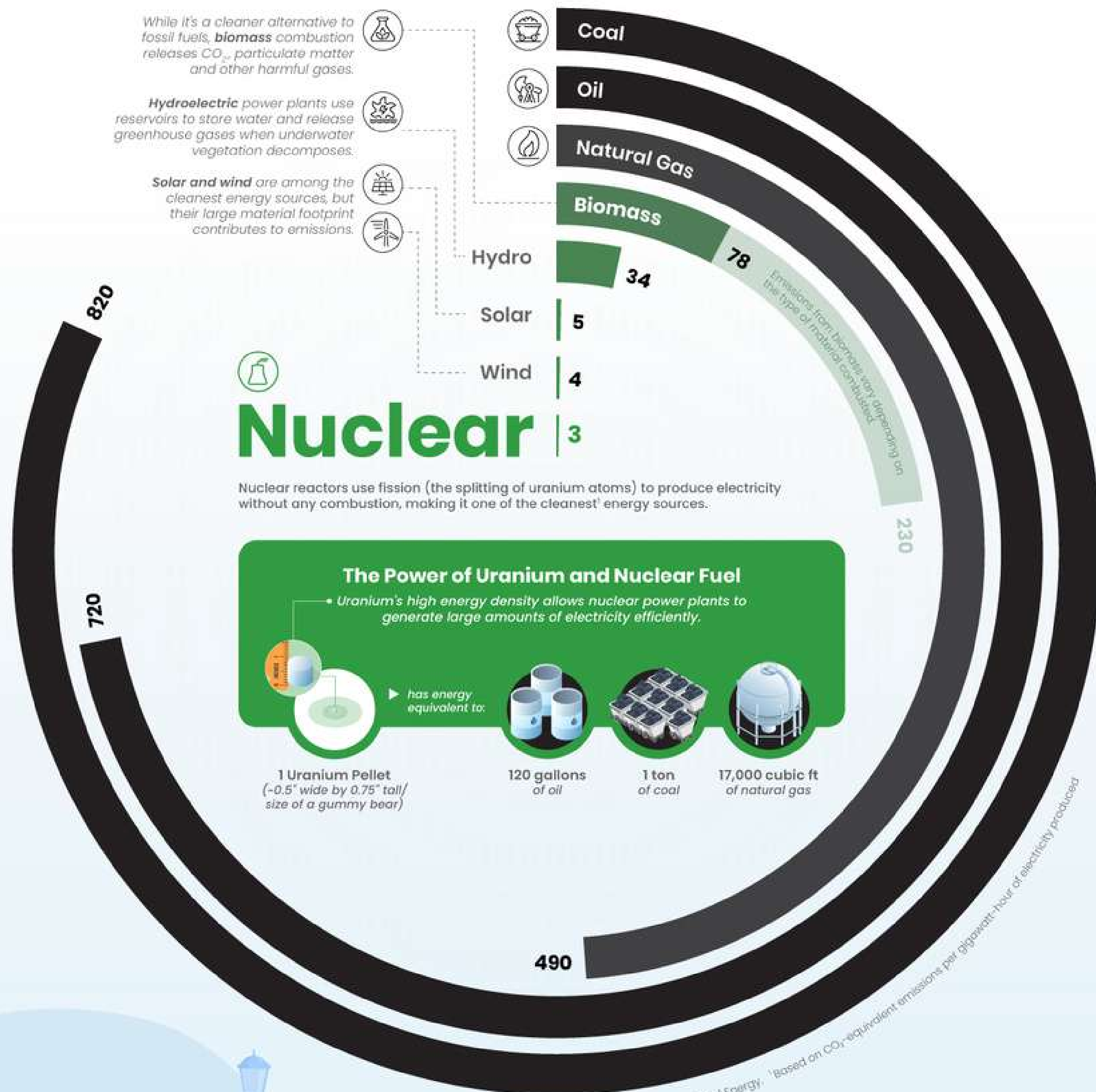
Images from: https://sprott.com/investment-strategies/physical-commodity-funds/uranium/

URANIUM

A KEY ELEMENT TO ACHIEVE A NET-ZERO CARBON FUTURE

The world is moving towards net-zero carbon energy. As populations and energy needs rise, energy sources of the future need to be both clean and sustainable.

Which energy source is the cleanest?



As one of the cleanest and most powerful sources of energy, nuclear power could play a key role in helping countries achieve decarbonization goals in the fight against climate change.

Sprott Physical Uranium Trust

The World's Largest Physical Uranium Fund*

TSX: U.U ($US) | U.UN ($CA) sprott.com/uranium

*Based on Morningstar's universe of listed commodity funds. Data as of 6/30/2021.
Important information about the Trust, including the investment objectives and strategies, applicable management fees, and expenses, is contained in the Management Information Circular.
View the Management Information Circular: sprott.com/media/4122/uranium-management-information-circular.pdf
Please read the document carefully before investing. Investment funds are not guaranteed, their values change frequently and past performance may not be repeated.

VISUAL CAPITALIST /visualcapitalist @visualcap visualcapitalist.com

7.

Carbon Credits

Carbon Credits have had a bad quarter, down roughly 15% in Q3. Year-to-date returns are down about – 12.5%. We're not happy about it but it is still up quite dramatically since we originally invested in early 2021.

The long term investment case grows stronger by the day. Carbon credits are in limited supply. The market is very short of supply at negative 25% this year and negative 35% next year. Real fundamental demand exceeds supply. We are likely in a recession brought on by inflation…We do not believe a recession will have a meaningful impact on the structural supply deficit in place in the carbon credit market.

8.

Precious Metals

Despite the recent selloff, Precious Metals have still widely outperformed most assets over the past 12 months. We continue to view Precious Metals as a very important component to our portfolios because they are not correlated to other asset classes.

I'm quoting here from page 18 of Incrementum's excellent 'In Gold We Trust' report. "The average annual performance from 2000 to 2022 is 9.2%. During this period, gold has outperformed virtually every other asset class and, above all, every other currency – despite significant corrections in the meantime."

Gold performance since 2000 in various currencies (%)

Year	USD	EUR	GBP	AUD	CAD	CNY	JPY	CHF	INR	Average
2000	-5.3%	1.2%	2.4%	11.2%	-1.9%	-5.4%	5.8%	-4.2%	1.4%	0.6%
2001	2.4%	8.4%	5.3%	12.0%	8.8%	2.4%	18.0%	5.5%	5.8%	7.6%
2002	24.4%	5.5%	12.3%	13.2%	22.9%	24.4%	12.2%	3.5%	23.7%	15.8%
2003	19.6%	-0.2%	8.0%	-10.7%	-1.3%	19.6%	8.1%	7.4%	13.9%	7.2%
2004	5.6%	-2.0%	-1.7%	1.5%	-2.0%	5.6%	0.8%	-3.1%	0.1%	0.5%
2005	18.1%	35.2%	31.6%	25.9%	14.1%	15.1%	35.9%	36.3%	22.8%	26.1%
2006	23.0%	10.4%	8.1%	14.3%	23.3%	19.0%	24.2%	14.1%	20.7%	17.5%
2007	30.9%	18.4%	29.2%	18.0%	12.0%	22.5%	22.5%	21.8%	16.9%	21.4%
2008	5.4%	10.0%	43.0%	30.5%	28.7%	-1.5%	-14.2%	-0.8%	30.0%	14.6%
2009	24.8%	21.8%	13.0%	-1.6%	7.9%	24.8%	27.9%	21.1%	19.2%	17.6%
2010	29.5%	38.8%	34.2%	13.9%	22.8%	25.1%	13.2%	16.8%	24.8%	24.3%
2011	10.2%	13.8%	10.6%	9.9%	12.7%	5.2%	4.5%	10.7%	30.7%	12.0%
2012	7.1%	5.0%	2.4%	5.3%	4.2%	6.0%	20.7%	4.5%	11.1%	7.4%
2013	-28.0%	-30.9%	-29.4%	-16.1%	-23.0%	-30.1%	-12.6%	-29.8%	-19.1%	-24.3%
2014	-1.8%	11.6%	4.4%	7.2%	7.5%	0.7%	11.6%	9.4%	0.2%	5.6%
2015	-10.4%	-0.2%	-5.3%	0.6%	6.8%	-6.2%	-9.9%	-9.7%	-5.9%	-4.4%
2016	8.5%	12.1%	29.7%	9.4%	5.3%	16.1%	5.4%	10.3%	11.4%	12.0%
2017	13.1%	-0.9%	3.3%	4.6%	5.9%	6.0%	9.0%	8.3%	6.3%	6.2%
2018	-1.5%	3.0%	4.3%	9.0%	6.8%	4.1%	-4.2%	-0.8%	7.3%	3.1%
2019	18.3%	21.0%	13.8%	18.7%	12.6%	19.7%	17.2%	16.6%	21.3%	17.7%
2020	25.0%	14.7%	21.2%	14.1%	22.6%	17.2%	18.8%	14.3%	28.0%	19.5%
2021	-3.6%	3.6%	-2.6%	2.2%	-4.3%	-6.1%	7.5%	-0.6%	-1.7%	-0.6%
2022 YTD	-0.7%	7.9%	8.9%	3.7%	1.3%	5.6%	10.6%	7.5%	3.7%	5.4%
Average	9.3%	9.1%	10.7%	8.6%	8.4%	8.3%	10.1%	8.9%	11.9%	9.2%

Source: Reuters Eikon, Incrementum AG, figures as of 05/18/2022

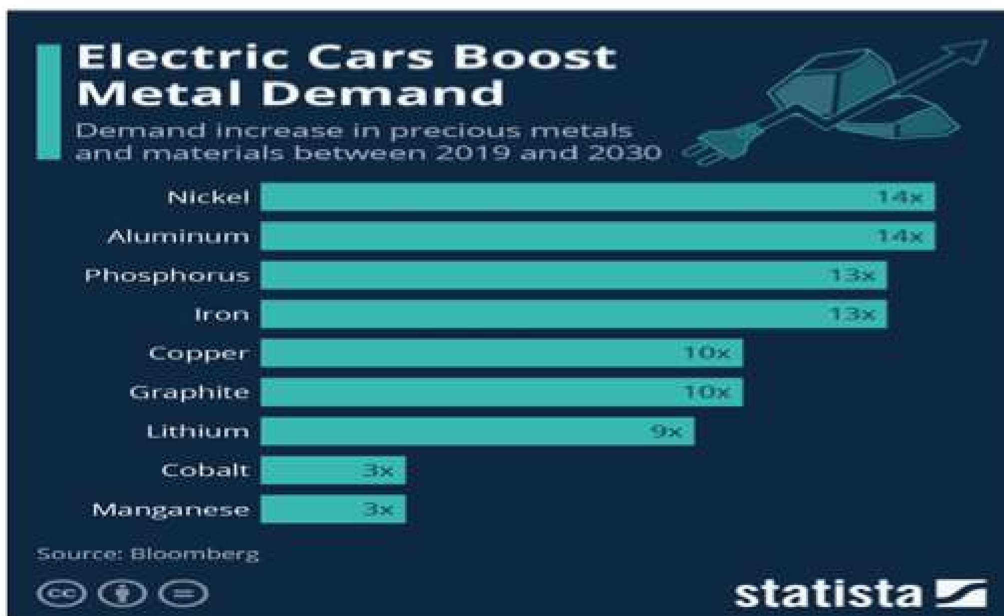
https://ingoldwetrust.report//wp-content/uploads/2022/05/In-Gold-We-Trust-report-2022-english.pdf

Gold has acted relatively strong in spite of a recent rise in real interest rates and in spite of a rise in the Dollar. If it can hold up relatively well in this environment then I believe it should have significant upside as other central banks play catchup with the FED and the Dollar turns down, particularly given that there are signs of speculative excess in the Dollar market.

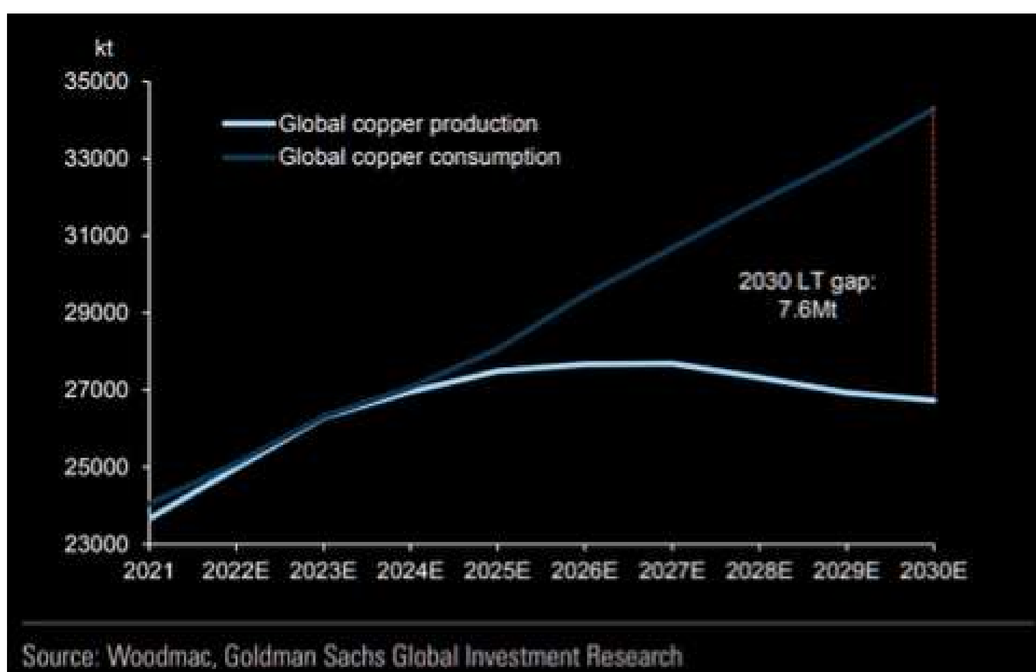
Precious Metals Mining Companies have had a rough year so far. We own two ETFs in the space, a Gold Miners ETF and a Silver Miners ETF. The Gold Miners ETF is currently down - 10.7% on the year and the Silver Mining ETF has posted a – 5.7% on the year. They are very volatile instruments. Central bank liquidity removal has not been kind to riskier assets and precious metals miners are considered some of the riskiest, but there are some great things happening fundamentally. Precious Metals Miners are extraordinarily attractive. In aggregate, the top 50 gold and silver miners by market cap on North American exchanges still trade at its highest free-cash-flow yield in history!

Precious metals mining companies' trade at extraordinarily cheap valuations, have excellent fundamentals and great balance sheets. There are broken stocks and broken companies/industries. However, when you see an industry like this in rude fundamental health, accompanied by a beat down stock, particularly in a sector that, on a longer term basis, has a low correlation to other industries and sectors, it's an opportunity, not a reason to sell.

Not all assets suit all investors, but where appropriate we have a selective focus in industrial metals. I showed this image last Qtr but it provides important perspective for the long term and adds colour to the commodity theme.



We have a long term view but we currently favour Copper most in the Industrial Metals space. Not that the other industrial metals are not compelling, but Copper is the largest, most liquid market in the space. In Euro-denominated terms it has lost 9.2% this year so we are not currently painted in glory with this position. For perspective though, that return is a lot better than many developed market equities and it has the same risk profile (a 6 on the ESMA scale). We've been a bit caught off-guard by the selloff this year because the fundamental picture is extraordinarily bullish, long term. The image below shows a gigantic long term supply gap between production and consumption.



9.
Conclusion

To conclude we've aligned our portfolios as best we can for a continued inflationary environment and will continue to have that stance until the data tells us otherwise. We think central banks will be forced to keep hiking interest rates until something breaks and with employment data still quite strong in the western world, we think central banks have strong reasons to continue with interest rate hikes and other forms of liquidity removal.

We think Crude oil is going to roar in the next 12 months and the knock on effect of that, is that central banks will have to be even more aggressive. We are trying our best to be positioned to benefit from that environment.

Again, I'm going to paraphrase Vincent Deluard, of Stone X from his Flow Show Report in italics below. I'm not quoting him word for word but its close enough to be considered plagiarising if I did not credit him. Vincent is the best macroeconomic analyst that I know of after the great Julian Brigden of MI2 Partners.

Inflation is the only way out for heavily indebted governments in slow growth economies. Inflation is a stealth tax. It causes incomes and revenues to increase. The knock-on effect of this is that tax receipts rise faster than nominal growth during periods of high inflation. Most debt is fixed debt. Debt that is locked in at a set rate for a set duration of time. So over time as inflation rises and the cost of the debt stays the same, the old debts become more easily serviceable and they get inflated away as happened in the decade following WW2. Even in the case where there is shorter duration debt or floating rate debt where inflation is uncomfortably high and central banks have to hike interest rates; As long as the inflation rate is well in excess of the interest rate, over time the effect is the same....Old debts become more easily serviceable and you eventually inflate away the debt burden.

Now there is no question that inflation is of great concern to voters and plenty of political heads will roll over rising prices, but do you honestly believe there is an alternative?

A decade of austerity in Europe has ruined southern ecoonomies and done very little to alleviate their public debt loads because the denominator (GDP) shrank at the same time as the numerator (public debt). Greece and Italy only recovered when (the head of the ECB at the time) Draghi announced that the ECB would effectively monetize European nations' public debt. Just as the Tea Party was the reaction to the careless accumulation of private sector debt in the 2000s, Modern Monetary Theory – inspired policies are the reaction to the nationalization of private debts in the 2010s.

There is no Tea Party today. Why would government officials fight price increases which make tax receipts grow faster than GDP? Inflation guarantees higher revenues for governments and therefore higher budgets for administrations, without the political pain of higher taxes.

There are only two logical outcomes in 2022.

1. Inflation slows as central banks have forecast and US/European economies fall into severe recession.
2. Central Banks avoid a recession, but inflation doesn't come down very much.

The lesser of the two evils points to outcome number two. Regardless, we are heartened by how well our portfolios at Baggot Investment Partners have performed relative to peers, in what has been an extraordinarily challenging environment.

Please do let us know if you wish to discuss your portfolio at any time. We appreciate your faith and trust in us.

Kind regards,
David Flynn
Chief Investment Strategist and Director
dflynn@baggot.ie

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