OYAT ADVISORS – QUARTERLY COMMENTARY

4Q 2023

Investment landscape

Market sentiment was more volatile than normal over the course of 2023, bouncing from recession worries and bank failures at the start of the year, to 'resilient growth' and the advent of artificial intelligence (AI) over the summer, to concerns about sovereign debt levels and interest rates remaining 'higher for longer' in the autumn, and eventually ending the year focused on falling inflation and growing excitement that central banks will cut interest rates sooner than previously expected.

As a result, the final stretch of the year saw strong returns across most major asset classes, including stocks, bonds, real estate investment trusts (REITs), precious metals, and cryptocurrencies. Only commodities were the outlier, with an altogether uninspiring year following a strong 2022.

This is the 'good' news in short: it was a positive year for the vast majority of financial assets. Let us now dig a little deeper into some of the more worrisome facts below the surface.

We might as well start with the banking crisis that occurred in March, which saw First Republic Bank, Silicon Valley Bank, and Signature Bank become insolvent and eventually fail; not to mention the overnight failure of Credit Suisse. As described in more detail in our 1Q23 commentary, due to rising interest rates, the value of banks' bond portfolios fell sharply, so that many small and regional banks found themselves in a vicious cycle of falling deposits and asset liquidations, which culminated with many such banks virtually on the verge of collapse. The three aforementioned U.S. institutions did eventually go bust, leading to over $500 billion in bank assets failing in a matter of days, surpassing the record from the global financial crisis of 2008.

Many more banks might have failed, if the FED hadn't intervened with a new facility, the Bank Term Funding Program (BTFP). This enables banks to borrow 100% of the face value of certain securities for up to a year. Usage of this facility rose sharply in March 2023, and then again towards the end of the year, reaching USD 136 billion as 2023 came to a close. This latest increase coincides with a widening arbitrage opportunity[1] - whereby banks can borrow from the BTFP at about 4.9% currently, and park that at the central bank to earn 5.4%, the interest on reserve balances. In other words, banks have benefitted from a risk-free arbitrage opportunity in order to help them shore up their balance sheets. This is just as well, since the BTFP is set to expire in March 2024, and unless interest rates fall substantially in 1Q24, the losses on banks' bond portfolios aren't going anywhere. Of course, as Milton Friedman once observed, *'nothing is so permanent as a temporary government program'*; still, there is some uncertainty about what banks will do come March, should this bailout program be shut down.

[1] https://www.bnnbloomberg.ca/use-of-fed-term-funding-tool-rises-to-record-in-arbitrage-play-1.2016169

Let us now turn to the state of the global economy. At the start of 2023, one of our chief concerns was the impact of tighter monetary policies by central banks on global liquidity, which is a key driver of global GDP growth (and asset prices). In our [4Q22 commentary](), we suggested that following inflation and interest rate shocks in 2021 and 2022 respectively, the next big risk facing investors was likely to be a recessionary shock.

A global recession, however, has not occurred for the time being. Why? First, because there is typically a time lag of one to two years for rising interest rates to impact economic activity, as households and businesses gradually have to refinance debts and adjust their behaviour.

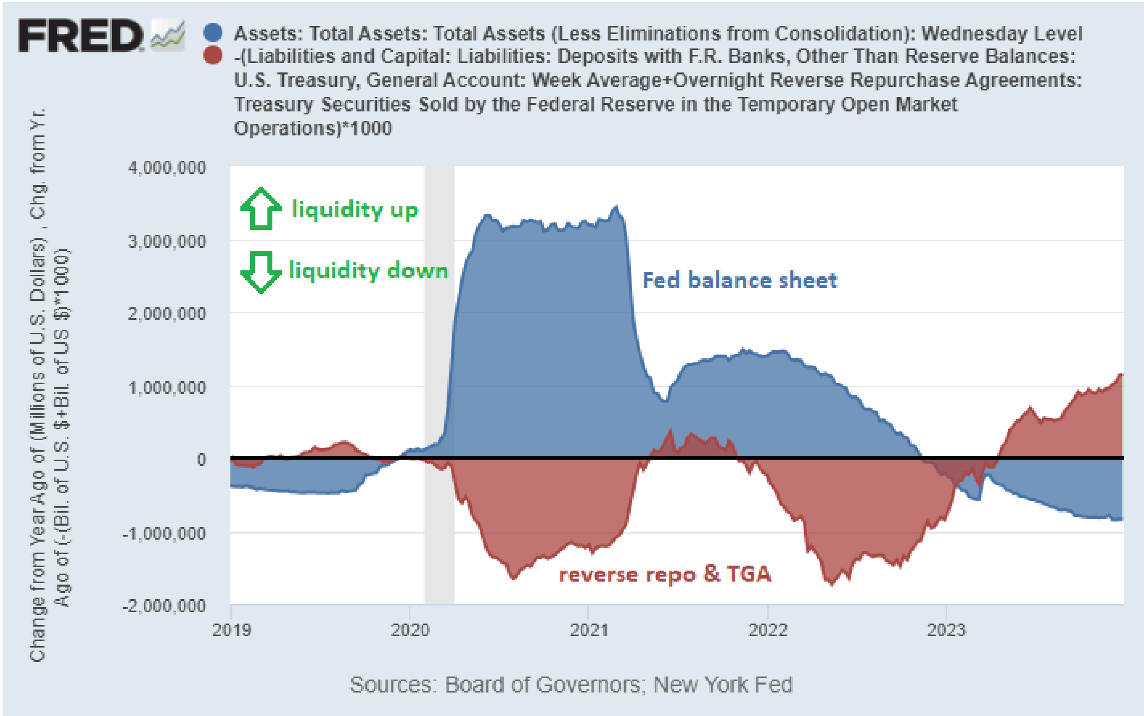
Perhaps more importantly, sovereign governments more than counterbalanced the liquidity contraction from monetary tightening by pulling their various levers to put liquidity back into the market. By and large, this has taken the form of deficit spending, which we highlighted in our [3Q23 commentary](). For fiscal 2023 (ending in September), the U.S. deficit amounted to USD 1.7 trillion, and closer to USD 2 trillion including student loan forgiveness, or over 7% of GDP.

Moreover, the U.S. Treasury decided to shift borrowing heavily into short-term bills, with an astonishing 85% of Treasury debt issues in 2023 due within one year or less. This had the knock-on effect of enticing money market funds to switch excess liquidity parked at the FED in reverse repurchase agreements (RRPs) back into T-bills, effectively pushing additional liquidity into the financial system.

Without going further into the weeds, it is important to realize that these rather uninteresting and technical details are significant, because we're talking about really large numbers. To add some perspective, the Treasury market now is 14% bigger than the entire U.S. banking system, according to Wells Fargo economists cited in a Barron's article last month[2]. In 2006, the Treasury market was only 44% the size of the banking system.

In a recent Seeking Alpha article[3], macro analyst Lyn Alden included a graph that does a great job at illustrating the overall impact of U.S. monetary and fiscal policies on total liquidity. As shown below, 2023 can be broadly characterized by some level of monetary tightening, which was more than offset by fiscal easing, for a net positive impact on liquidity. This had a significant short-term positive impact on the global economy and financial markets, though the longer-term consequences of these actions are likely to be detrimental.

[2] https://www.barrons.com/articles/u-s-treasury-massive-stock-bond-repeat-3c3580b4
[3] https://seekingalpha.com/article/4661453-fiscal-and-monetary-divergence



Source: Lyn Alden Seeking Alpha article

Finally, let's briefly discuss inflation and the growing expectation that central banks will soon start to cut interest rates. We explored the topic of inflation in some detail in our [2021 Annual report](#) (pg. 7-10). Let us add to that by making a number of observations.

First, it is important to understand the base effect in interpreting the declining rate of inflation. Prices are still increasing, but at a slower rate, partially due to a higher baseline. Cumulatively, the consumer price index (CPI) is up nearly 20% since the start of 2020. So, while the rate of inflation is coming down, inflation is still a real concern for many people.

Second, we appear more cautious than some in assuming that the fight against inflation is over and done with. Considering the current rate of positive growth in global liquidity, we find it difficult to see inflation decline much further towards its stated target, barring a deflationary recession, which may still occur. But overall, considering the likely interest rate cuts in 2024, as well as a possible phasing out of quantitative tightening[4], we would not be overly dismissive of the chance that inflation starts accelerating once again. After all, it isn't uncommon to have periodic disinflationary episodes throughout longer periods of structural inflation, as occurred during the 1970s.

[4] https://www.reuters.com/markets/us/deflating-qt-cushion-may-have-raised-red-fed-flag-mike-dolan-2023-12-06/

Financial markets

From the global economy avoiding a recession to the massive stock market rally, 2023 defied many people's expectations. Heading into the year, many investors expected volatility in financial markets, and the potential for further price declines from an already difficult 2022. The outlook for stocks appeared challenged, as the FED was continuing to raise interest rates at a rapid pace, and many investors felt that a recession was likely just around the corner. Even those in the more optimistic camp predicted tepid gains at best for 2023.

Instead, 2023 turned into one of the best years for stock market performance in the past decade. In a dramatic reversal of fortunes, it was a particularly strong year for certain technology stocks and other 'growth' companies that suffered the biggest losses in the 2022 market collapse.

Stock market index	2023 performance (in local currency)	10y bond	Yield	Yoy change	FX	Yoy change	Precious metals	Yoy change
MSCI World (USD)	24%	US	4.05%	22 bps	USD Index	-2.0%	Gold-USD	12.8%
Dow	14%	Germany	1.11%	-145bps	CHF-USD	9.8%	Silver-USD	-1.2%
S&P	24%	Italy	3.66%	-93 bps	EUR-USD	3.2%		
NASDAQ	43%	Switzerland	0.83%	-79 bps	GBP-USD	5.3%		
Stoxx	13%	UK	3.87%	20 bps	JPY-USD	-7.0%		
SMI	4%	Japan	0.61%	20 bps	CNY-USD	-2.8%		
FTSE	4%				RUB-USD	-17.5%		
Nikkei	29%							

Source: LSEG Refinitiv. All data as of Dec. 31st 2023.

The poster child for the 2023 rally is semiconductor chip designer Nvidia, whose stock rallied a gigantic 239%, as the emergence of AI disrupted the technology landscape. In the prior year, Nvidia's market value had dropped by about 50%.

Overall, technology stocks posted a huge year, surging 59%, or their best performance since 2009, according to Morningstar[5]. The so-called 'Magnificent Seven' stocks generated a 75% return for the year, versus 24% for the S&P 500; so without them, the index would have risen just 12%, according to calculations by Neuberger Berman[6]. By the end of 2023, the cumulative weight of these seven stocks represented close to 30% of the S&P 500.

While the rally in stocks did broaden towards the end of the year, 2023 ranked as the second worst year in decades for value vs. growth stocks[7]. For instance, the MSCI World Value Index posted a modest 9% gain, while its 'growth' counterpart soared by 36%.

Moving on to bonds. The broad fixed-income market looked on pace for a third consecutive year of losses, as uncertainty around a 'hard' or 'soft' landing lingered and interest rate volatility persisted. But with a significant year-end rally due to the FED's shift in policy, the bond market eventually managed to eke out some small gains for most investors.

5 https://www.morningstar.com/markets/15-charts-surprise-everything-rally-2023
6 https://www.nb.com/en/global/equity-market-outlook/equity-market-outlook-1q2024
7 https://finimize.com/content/value-vs-growth-stocks-which-ones-to-favor-in-2024

Currencies were extremely volatile throughout 2023. Following two years of gains, the dollar index declined by 2% in 2023, driven by rising debt levels, a credit downgrade by Fitch in August, and growing expectations that the FED will start cutting interest rates in 2024. Relative to the U.S. dollar, Japan had the worst performing currency among G10 nations for a third consecutive year, as it held out as the only central bank maintaining a negative interest rate policy. On the other hand, the Swiss franc was the strongest performing G10 currency for the second year in a row, followed by the British pound and the Euro. The currencies of Sweden, Australia, Canada, New Zealand and Norway also performed well.

Last, looking at the precious metals market, gold rose 13% (in USD) in 2023, hitting a record high in December. This might have surprised a number of investors, who supposed that gold might decline as a result of higher real interest rates, as observed historically. But it appears that this was more than offset by rising overall global liquidity, robust buying from a number of central banks, as well as persisting geopolitical risk. On the back of these dynamics, the price of gold is expected to test new all-time highs in 2024. Silver, on the other hand, did not rally alongside gold throughout 2023. The gold to silver ratio increased to 86.5 by year end - a fairly elevated level, although still way short of the 125 reached in March 2020.

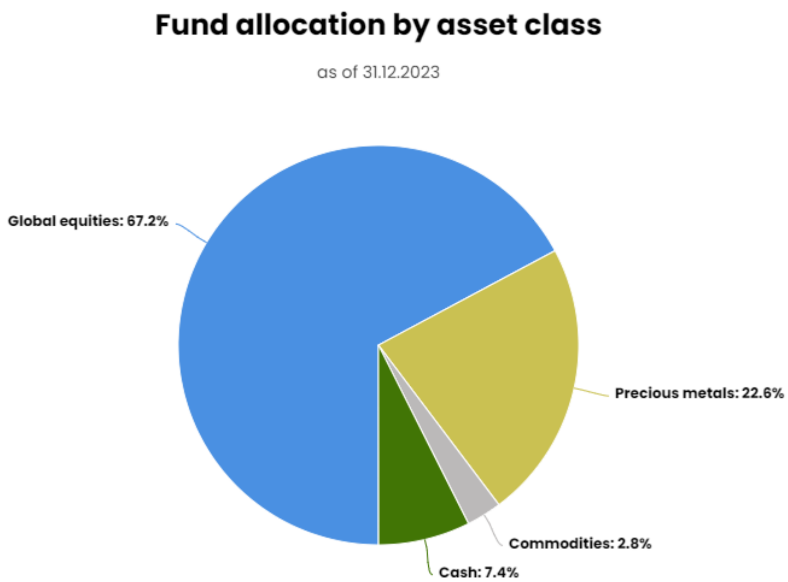
In conclusion, today's investment landscape is a fairly tricky one to navigate. On the one hand, markets - as represented by their benchmark indices - appear priced for perfection, with asset prices reflecting a substantial number of interest cuts in 2024, as well as a 'soft' landing of the global economy. On the other hand, there are valid concerns to be had about rising debt levels, geopolitical risks, the possibility of an economic recession, as well as the future trajectory of inflation. On the latter, we believe that it is far from impossible that we are currently experiencing a period of temporary disinflation, in an overall long-term inflationary era which may last for some years to come.

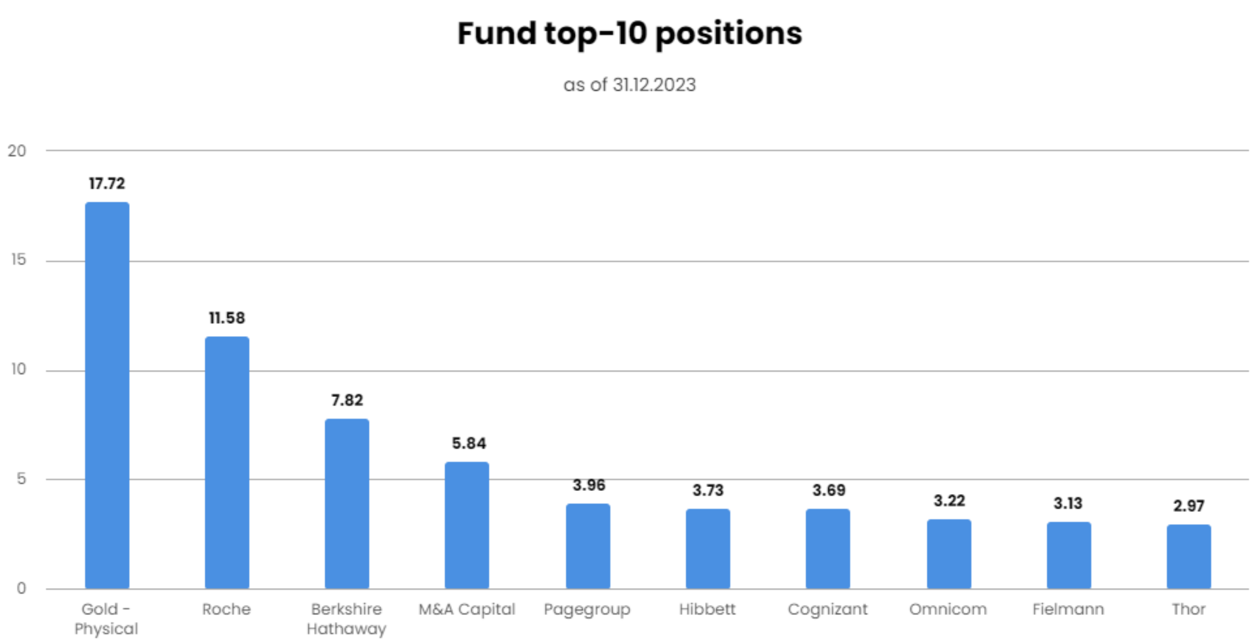
In times of structural inflation, the nominal price of productive and real assets typically perform quite satisfactorily, whereas the performance of fixed-income securities and cash suffers, especially in real terms. With that in mind, let us reiterate what we've stated incessantly over the past couple of years: in a world of monetary abundance, we want to mainly focus on owning scarce and productive assets, thoughtfully selected on the basis of our investment process that focuses on quality businesses trading at reasonable prices. We also want to maintain some level of optionality by holding liquid reserves, predominantly in the form of physical gold.

This continues to be the case as of today.

Asset allocation

The graphs below display the Oyat Investment Fund's allocation of capital across asset classes, as well as the Fund's top-10 positions:





<u>Performance</u>

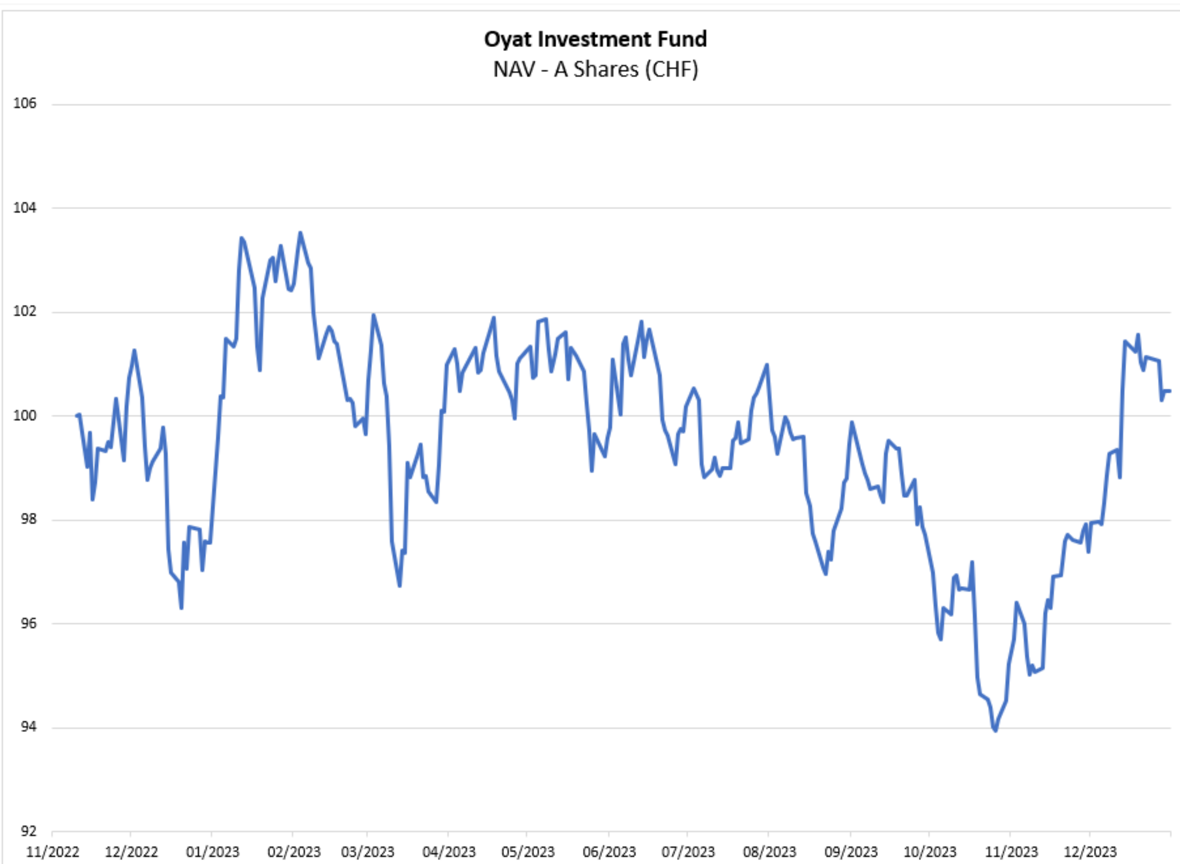
Performance as of December 31, 2023, in CHF

	3m	1yr	3yrs p.a.	5yrs p.a.	Since inception p.a.
Oyat Investment Fund	2.8%	3.0%	-	-	0.4%
MSCI World	2.6%	13.3%	-	-	4.4%

Annual performance as of December 31, 2023, in CHF

	2022*	2023	Cumulative*
Oyat Investment Fund	-2.4%	3.0%	0.5%
MSCI World	-5.0%	13.3%	7.6%

**Inception Date: November 10, 2022*



In the fourth quarter of 2023, the Oyat Investment Fund returned 2.8% in CHF, versus 2.6% for the MSCI World Index.

For the full calendar year, the Fund returned 3.0% in CHF, versus 13.3% for the aforementioned reference index.

Since inception, the Fund's total annualized return stands at 0.4% vs. 6.7% for the index.

It is likely that some may be somewhat underwhelmed with the Fund's rather uninspiring performance this past year. This is especially the case when measuring investment results in Swiss Francs, as we do, which was once again particularly strong in 2023. For the benefit of our non-Swiss investors and readers, it may be useful to detail that while the Fund returned 3.0% in Swiss Francs this past year, this figure stood at 9.7% in Euro, and 13.1% in U.S. dollars.

Furthermore, investors who focus on relative performance may be disheartened to see a sizable gap emerge between the Fund's performance and the reference index. Without being overly dismissive of this, let us reiterate a number of important facts that may help readers understand why this has happened.

First and foremost, it is critical to bear in mind that we are principally focused on absolute returns, in-line with our main objective of capital preservation and appreciation in real terms. What this means in practice is that the Fund's assets are managed independently of the reference index. We do not base asset selection on what the reference index owns, rather focusing on our own bottom-up investment process. Ultimately, this leads us to construct a portfolio of assets that bears little to no resemblance to the index. As a case in point, the Fund's active share since inception stands at nearly 97%. In other words, the Fund's overlap with the reference index is only approx. 3%. So, while the MSCI World arguably remains the most appropriate index to benchmark the Fund's investment performance, it is important to understand that it is far from a perfect yardstick.

Consequently, it goes without saying that different portfolios necessarily imply different risk profiles. And while people are quick to compare the performance side of the equation, they rarely focus on the level of risk assumed, which is more difficult to assess, let alone measure accurately. Yet, we are convinced of the fact that the Oyat Investment Fund assumes a much lower level of risk than the MSCI World Index, as defined by the probability and magnitude of a permanent impairment of capital (rather than volatility). This is due to our focus on owning fundamentally higher-quality companies compared to the index, which we purchase and own at reasonable prices, providing us with an additional margin of safety. Lastly, our physical gold position, which is the largest in the Fund, represents the ultimate risk-free asset, and obviously goes a long way in reducing the Fund's overall risk profile.

Finally, we strongly encourage readers to focus their assessment of performance, both absolute and relative, on the long-term. We recognize that this might be difficult, in a world that is increasingly bent on instant gratification, and in which *'being early is the same as being wrong'*. But it is key to understand that only over the long-term can performance be assessed in isolation of transitory events that can positively or negatively impact results.

Let us now briefly discuss some of the Fund's main performance contributors and detractors for 2023. Please note that all return figures quoted below are in Swiss Francs.

Fortunes changed rapidly in the athletic footwear retail space, which uncharacteristically saw both our largest performance contributor and detractor for 2023. On the one hand, our position in Hibbett - added to the portfolio at a very attractive price throughout 2Q23 - returned a handsome 87.7% last year. However, our legacy holding in Foot Locker declined by 52.1% between the start of the year and our eventual divestment of the company, as the company struggled to implement its turnaround plan, while Hibbett continued to execute well on its strategy. In our opinion, Hibbett remains attractively priced as of today, although with a slightly smaller margin of safety.

The Fund's performance this past year was also impacted by weakness in our large Roche position. As we've described in our prior commentaries, Roche has been out of favor as the company's diagnostics business has declined from a pandemic-driven peak, while pipeline disappointments in both the Alzheimer's area and the company's TIGIT cancer immunotherapy trials have left growth expectations in the doldrums. But long-term fundamentals remain largely unchanged, as these setbacks do not materially impair Roche's deep research and development capabilities, that few peers can match. Roche's stock, which declined by 12.8% in 2023, now trades toward the bottom end of its historical valuation range, with a forward PE of about 13x, a forward free cash flow yield in excess of 7%, and a dividend yield of close to 4%. This strikes us as a very attractive price level for a defensive, high-quality company such as Roche. Going into 2024, we feel very comfortable having it as our largest single stock exposure.

Lastly, we also suffered some likely temporary drawdown in our Franco-Nevada position, which declined by 25.4% in 2023. This results from the long-standing legal dispute between First Quantum and the government of Panama surrounding the Cobre Panama mine, which Franco-Nevada has a stake in. For those interested in the details, we wrote an article on the topic earlier in the year. What has transpired since is that only a few months after a deal had been reached for a new operating contract, Panama's Supreme Court ruled the contract unconstitutional, and ordered the mine's closure. We believe that there is still a chance that the situation normalizes itself, and operations resume in good order. Alternatively, it looks clear that First Quantum will take up the matter in front of the International Court of Arbitration, and seek to be compensated for the expropriation of its assets by the Panamanian government. While it might take a number of years, this would likely result in a favorable outcome for First Quantum, and thus Franco-Nevada. As Franco-Nevada's share price decline essentially reflects a total loss of the asset, while we believe the recovery value to be not insignificant, it appears to us that this situation has created an interesting buying opportunity in the stock.

Moving on to the good news and performance contributors. We've already mentioned Hibbett, which was our largest performance contributor in 2023. Thor Industries also performed well, returning 45.3% during the year, as the producer of towable and motorized recreational vehicles once again proved its ability to manage difficult market conditions and maintain good levels of profitability, even when revenue declines. The industry leader in what is essentially an oligopoly experienced substantial revenue growth during the pandemic as people looked to recreational vehicles to take vacations, and with hotels closed and urban spaces under lockdown. Remote working made life on the road easier as well. As uncertainty around the sustainability of Thor's revenue and profitability pushed the stock down at the end of 2022, we were able to purchase the quality company at an attractive valuation. Recent reporting did show a meaningful drop in revenue, but the company's flexible cost base allowed Thor to keep profits higher than expected, driving the stock price higher.

Last, Société pour l'Informatique Industrielle (SII) is a small French technology consultant and technology services company, which we only added to the Fund in 3Q23, based on what we considered to be strong business fundamentals, an attractive valuation level, and a strategic family ownership. However, a few months later, the company announced a simplified tender offer, effectively taking the company private while Blackstone - one of the world's largest alternative asset manager - enters the firm's capital structure. Disappointed though we were to see our ownership of SII be prematurely ended, the 45.6% return was a welcomed contributor to the Fund's performance in 2023.

In closing, we should mention the addition of Société Générale de Surveillance (SGS) to the Fund in December 2023. SGS is the largest of a number of firms operating in the testing, inspection, and certification (TIC) market, which we believe to be fairly attractive due to relatively stable revenues, a number of structural growth drivers, and an industry structure that is both consolidated at the top and very fragmented at the bottom, which creates the opportunity for acquisition-led growth. SGS is the more conservatively run company in this market, being largely focused growing its business via organic investments, and returning excess capital to shareholders via dividend (currently over 4.5%). Following a decade of being arguably overvalued, we believe that SGS is now finally trading at a fair price once again, and were happy to add it to the Fund's holdings. Readers interested in more details on our investment case for SGS should refer to a recent article on the topic.

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