

The Weekly Beacon

We will be giving some macro economic market updates on a weekly basis. No equity recommendations will be given in this commentary, and we encourage you to contact us if you have questions regarding any observations.

*The two main purposes of a Lighthouse are **to serve as a navigational aid and to warn ships (Investors) of dangerous areas.** It is like a traffic sign on the sea.*



Lighting of the Lighthouse, Christmas 2021, Edgartown, Massachusetts



Montauk Lighthouse, New York

Feel free to send us your photos of Lighthouses to be featured in our weekly market observations.

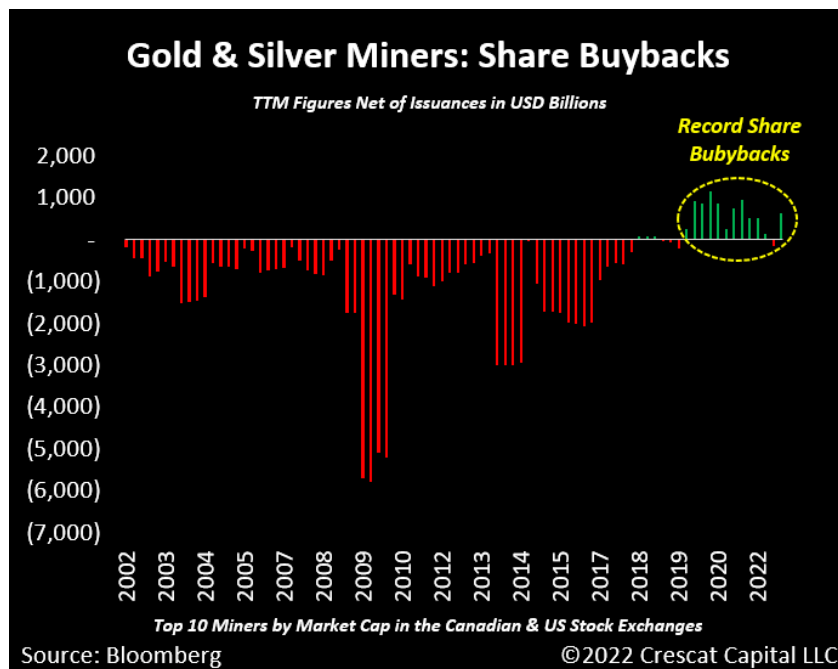


Mining Reversal

2022 brought us sky high inflation, World War 3 worries, supply chain gridlock, and many more global issues. In theory, it was a perfect year for holding gold as an asset. The only issue is sometimes theory does not equate to reality.

Even though gold held its value and was not down nearly as much as stocks, bonds, and other assets, we think it underperformed itself in similar years. We think gold prices could lead the way in 2023 after a year of consolidation. Even though some claim gold as a failure in 2022, we think holding gold was a major win on a relative basis. The U.S. Core Aggregate Bond ETF (AGG) is down 12% YTD, the S&P 500 is down 17.4% YTD, and Bitcoin (new gold) is down 62% YTD. When you compare those returns to gold's YTD (down 5% (as of December 6th)), there is no comparison, maybe 2023 is when investors will realize gold is a great piece of a portfolio. We are certainly not advocating for the entirety of a portfolio to be in gold or for it to be the largest position, we just think it belongs in an investors portfolio especially going forward.

Now that we got some of our macro thoughts on gold out of the way. We share with you a chart that is quite bullish for gold mining equities moving forward.



For the first time in 22 years, a major trend has changed in this sector. The allocation of capital has dramatically shifted, instead of raising equity miners are buying back stock. This means the largest miners are buying their stock from the stock market. This elevates the demand for shares and increases the stock price (Economics 101). The other way this trend helps long-time shareholders is their shares do not get diluted as more equity is not being issued.



So why does this matter, many large miners have the cash flows to be able to afford to buy back their stocks which means they are financially healthy. This is important across the mining sector due to the volatility of commodity prices as well as the nature of the business which is capital intensive.

With all that being said, we are not naive and understand equity (new shares) is not being issued due to where we are in the capital markets cycle. It is not in a firm's interest to issue new capital in today's market conditions. So, a bit of this chart could be misleading. However, this trend has been going on for the last few years and we think it will continue. We think this indicator will be yet another bullish signal for the sector going forward.

Value Stocks Winning

Since November 2021 a trend began. Value stocks on the S&P 500 outperformed growth on a relative basis. We think this could continue going forward, especially with interest rates remaining elevated, inflation remaining high and economic worry present across markets.

The last two times this trend happened it was not for 1 year; it was for numerous years. From 1975-1989 and 2000-2007, investors would have benefited from being in value stocks. After a 14-year period where growth stocks outperformed value, we think we are turning the corner.



Even without this chart, we are sure you know how explosive markets were from 2011-2021, returns were astronomical, the capital was inexpensive, and everything performed well. This happened because interest rates plummeted, and the printers were left on overnight (for 15 years straight). It's no surprise that at soon as liquidity dried up in 2022, the asset classes that benefited from inexpensive money were



the ones that completely collapsed (SPACs, crypto, high growth / unprofitable tech companies). Those things only boomed on speculation and an influx of liquidity. How else do you explain how Crypto started at \$0 in 2012 and is now worth close to \$1 Trillion (peaking at \$3 Trillion)? Crypto's boom was fueled by the FEDs' creation of inexpensive money.

Besides the liquidity argument, we do think value stocks will outperform growth stocks and would expect this chart to continue going forward. That does not mean every value stock will be a winner and every growth stock will be a loser. Stock selection will be very important in the next cycle.

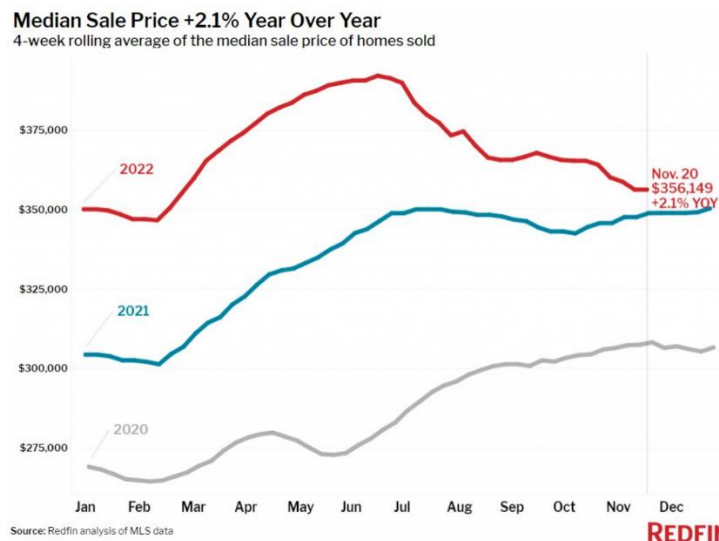
This is purely an overarching theme that we wanted to communicate to you. We are not recommending any ETFs with these comments. Contact us today, with any stock or fund-specific questions @ info@macnicolasset.com (Canada) and info@macnicol.com (US).

So, you're saying you want to buy a home?

A lot has been said in the residential housing sector this year. We are here to help you navigate through what is real and what is not. To preface, being bullish on an area (geographic) does not mean that is our thought on the sector. This is also an overview of only residential, it does not mention retail, industrial, office, or any other type of real estate. We are sure if you read our [Alternative Asset Trust Commentaries](#) that you know we have increased our industrial real estate exposure in the MAC 360 Degree Real Estate Fund. This commentary also has nothing to do with the real estate market north of the border.

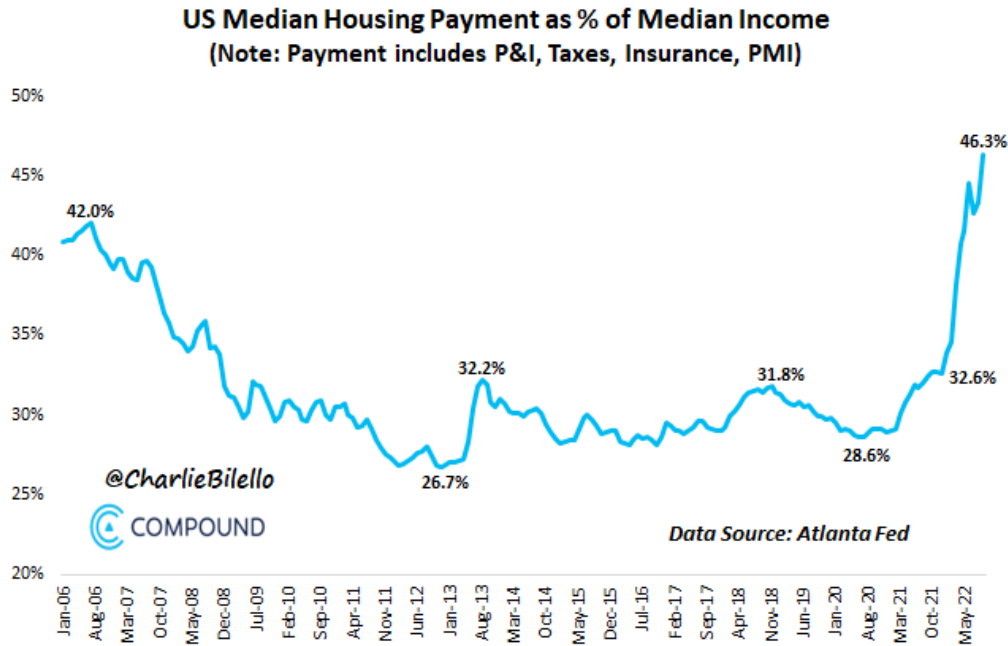
Jumping into the raw data, what has happened?

Despite the narrative and home prices retreating since the summer, median U.S. home prices are up over the last year.





Home prices have recently declined, but they also surged for 2 years straight (mid 2020-mid 2022), something that was unsustainable. The decline in home prices is mainly due to an increase in interest rates which have made homes pricier for consumers. Consumers are paying the most they ever have for their mortgage (on a percentage of total income earned).



The average American with a mortgage is paying 46% of their monthly earnings just for housing. This is much higher than in any period over the last 15 years. This is also 20% higher than during Covid-19. Mortgages have grown due to home prices which increase monthly payments, but the interest associated with mortgage payments has ballooned in the last 4-6 months (as the FED increases interest rates to fight inflation). So, consumers are being stretched on housing just like they are on their energy bills, gas pumps, grocery stores, and restaurants. An expensive time to be a consumer. An especially expensive time to be a retired consumer on a fixed income.

Finally, where have prices changed the most since prices have dipped? It seems the west coast and larger Northern cities. The housing markets the most off their all-time highs are mainly across California (San Francisco, San Diego, Los Angeles), other west coast cities (Portland, Seattle), and northern cities (Detroit, Boston, Minneapolis). Interestingly enough, the west coast housing markets peaked first and were the first to fall due to higher prices and low demand. It is also extremely expensive to live in many west coast cities, especially across California.



@CharlieBilello		Case-Shiller US Home Price Indices (as of September 2022)						Data: YCharts		
City	1-Year %	3-Year %	5-Year %	10-Year %	15-Year %	20-Year %	All-Time High Date	Months From High	% Below All-Time High	
Miami	24.6%	64.7%	77.7%	171.0%	62.7%	192.2%	7/31/2022	2	-1.0%	
Tampa	23.8%	69.8%	89.3%	182.9%	81.5%	191.6%	7/31/2022	2	-1.4%	
Charlotte	17.8%	55.3%	70.9%	123.9%	92.2%	139.4%	7/31/2022	2	-1.1%	
Atlanta	17.1%	50.4%	65.8%	145.3%	73.6%	101.5%	7/31/2022	2	-0.8%	
Dallas	16.3%	52.5%	64.1%	144.5%	137.3%	157.9%	6/30/2022	3	-3.7%	
Las Vegas	13.0%	48.4%	73.4%	197.6%	36.2%	141.2%	6/30/2022	3	-3.6%	
Phoenix	12.6%	66.8%	89.3%	172.4%	60.7%	181.7%	6/30/2022	3	-4.5%	
Cleveland	10.6%	36.5%	47.9%	72.0%	49.7%	57.8%	7/31/2022	2	-0.4%	
New York	10.6%	35.6%	41.6%	67.3%	33.4%	94.1%	6/30/2022	3	-1.4%	
Chicago	10.0%	28.7%	33.1%	64.2%	14.7%	48.9%	7/31/2022	2	-0.7%	
San Diego	9.5%	50.4%	60.6%	148.7%	79.3%	161.8%	5/31/2022	4	-6.9%	
Denver	9.3%	40.8%	56.1%	137.2%	130.3%	151.0%	5/31/2022	4	-4.5%	
Los Angeles	8.8%	38.8%	49.0%	130.3%	58.3%	184.7%	5/31/2022	4	-5.5%	
Boston	8.8%	37.0%	49.2%	97.2%	81.5%	109.1%	6/30/2022	3	-2.6%	
Detroit	8.0%	32.3%	45.8%	117.6%	55.9%	47.3%	5/31/2022	4	-1.8%	
Portland	6.7%	36.0%	46.9%	134.0%	77.6%	189.7%	5/31/2022	4	-4.2%	
Washington	6.6%	28.9%	36.4%	59.5%	33.2%	111.3%	5/31/2022	4	-2.2%	
Minneapolis	6.5%	28.3%	42.0%	88.2%	43.9%	70.0%	6/30/2022	3	-1.4%	
Seattle	6.3%	45.2%	60.4%	163.4%	95.2%	219.8%	5/31/2022	4	-8.7%	
San Francisco	2.4%	30.8%	42.4%	146.8%	71.6%	144.1%	5/31/2022	4	-10.3%	
20-City Index	10.5%	40.7%	51.4%	112.7%	58.4%	130.3%	6/30/2022	3	-3.3%	

Why do we care? This continues our firm's thesis and concentration on various southern metropolises. These areas have seen the smallest price dips in recent months, and they continue to exhibit the macro attributes that made them attractive, to begin with.

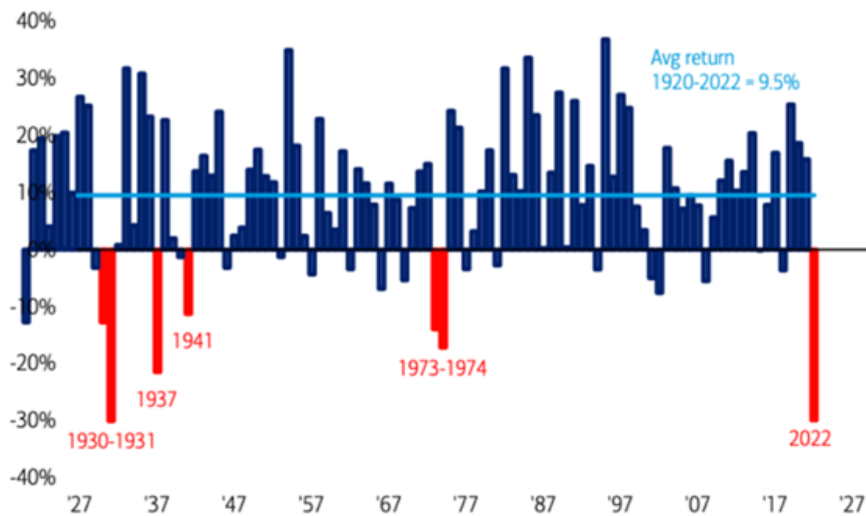
Failing Investors

The large banks and financial planners that continue to push 60/40 equity-fixed income strategies on their clients, continue to fail their clients. We are sure that those investors have been endlessly calling their advisors and are fed up with their portfolios. The only issue, these large institutions will not change, and their clients will be the ones stuck in a pickle.

The 60/40 strategy was implemented to give investors upside, yield, and safety, it has historically been known as a balanced portfolio.

When equity prices fall, fixed-income prices were supposed to perform extremely well (hence the term balanced). During these down years for stocks, bonds were supposed to make up for the shortfall in a portfolio. This strategy was successful for decades and investors benefited greatly from it. The only issue was in 2008 this strategy began to fail. Even though returns for a 60/40 portfolio have been mostly positive since 2008, they have lagged equity returns and the fixed income portion of the portfolio has not performed well in periods when stocks fell (2008, 2018, Covid-19 Crash, and 2022). This means in any given year; an investor may have to delay retirement due to the failure of this investment strategy.

Chart 3: Worst annual returns for “60/40” portfolio in past 100 years
Annual “60/40” portfolio performance (%)



Source: BofA Global Investment Strategy, GFD Finaeon. 2022 estimate is annualized as of October.
BofA GLOBAL RESEARCH



We do not think the performance of the 60/40 will look like 2022 (worst performance ever) going forward but think it could have some negative returns especially if yields continue to rise and stocks continue to struggle (very possible for years to come).

This failed strategy and the failure that has been traditional fixed income is why we are large believers in Alternative Assets as well as Alternative Debt Strategies. There is money to be made on the debt side that benefits investors, but many advisors just ignore it or do not understand the non-traditional debt strategies. That is why in 2023 we will be launching our Alternative Debt Fund to pair with our award-winning Alternative Asset [Trust \(click here to learn about our alternative asset program\)](#). Stay tuned for more information.

Senate Decided

The U.S. Senate had its last seat decided on Tuesday. In a runoff election just weeks after the midterms Senator Raphael Warnock defeated Herschel Walker to grab the 100th seat in the Senate. What does this mean? Democrats hold 51 out of 100 seats. It also means Democrats only need 1 of Joe Manchin or Krysten Sinema to vote for their agenda (Sinema and Manchin have been the most moderate Senators over the last 2 years and have been internal hurdles for Biden and his Administration). We called Senator Joe Manchin the most powerful Joe in the world last year as he essentially could get whatever he wanted from his party and veto anything that went too far.

Georgia ▾

Candidates	Vote %	Vote count
 Raphael Warnock Democratic Party	51.4%	1,817,479
 Herschel Walker Republican Party	48.6%	1,719,879



Now it looks like Sinema, and Manchin together will be the two biggest hurdles in the Senate. However, the next 2 years will not be near as smooth for the Biden Administration as the House belongs to the Republicans and they will try not to approve anything that they do not like. They will also steer the national conversation through committee hearings of their own.

We do not get into politics and explain what can happen in markets through every result, we just wanted to highlight a split Congress. Historically a split Congress is the best for financial markets. Equity markets on average perform best with a split Congress. We call this Washington gridlock and think the stalemate is good, especially when both U.S. parties like to go to extremes on their side of the aisle. Markets may benefit from a moderate leader who is close to straight down the road. Perhaps a return to predictability is on the docket for 2024 or 2028.

Bank of Canada Hikes Again

The Bank of Canada announced that it will raise its overnight interest rates by 0.5% raising the rate to 4.25%. This is the highest level for the overnight lending rate since 2008. The interest rate hike was on par with analyst expectations. At the announcement, the Bank of Canada used language that would suggest larger rate hikes are behind us and a potential pause in January is likely.

Bank of Canada Hikes Rate to 4.25%, Signals Potential Pause

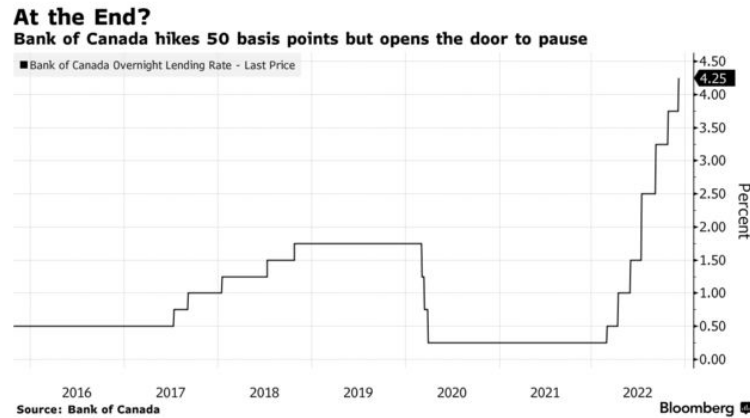
- Macklem raises by 50 basis points as economic momentum slows
- 'This is a pivot,' says Mendes, predicting no January hike

This lines up with many of our recent predictions. We said a pause was coming by western central banks sooner than many think. After a pause, one central bank will blink on recession fears and will begin to slash interest rates and reverse monetary policy (welcome back easy money). However, many analysts think the pause period will last quite a long time to reduce inflation.

We all know inflation will take time to come down and all understand that certain inflation is supply-driven and interest rate increases will have a smaller impact on reducing those specific prices. Sure, home prices have dropped but grocery, energy, rent, and gas bills have not. Buckle up, necessity

inflation will remain elevated, and luxury inflation will more than likely be the most impacted in the short term with these interest rate hikes.

Interest rates in Canada are now double what they were pre-Covid-19.



Canada's yield curve inversion hit its widest since the early 1990s this week, a global phenomenon that often precedes a recession.

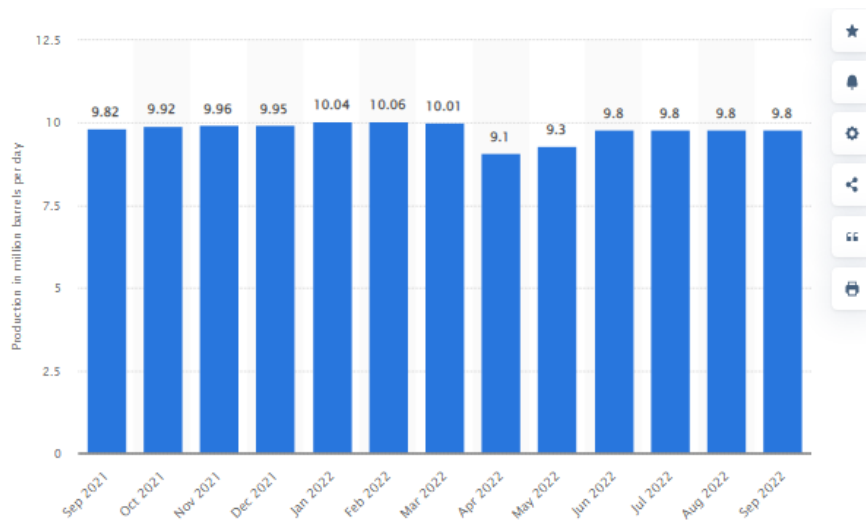
Energy Market Continues to Drop

Retail gasoline prices have retreated for 5 months in a row. Global crude and Brent prices have also significantly dropped from their 2022 highs. Western governments have claimed victory against energy prices. They believe their work has reduced Putin's power and Russia's strength. Even with oil trading in the mid-\$70s Russia is still printing money. They have relatively low costs in oil production.

Oil and gas barrel production Cost US\$, March 2016^[99]

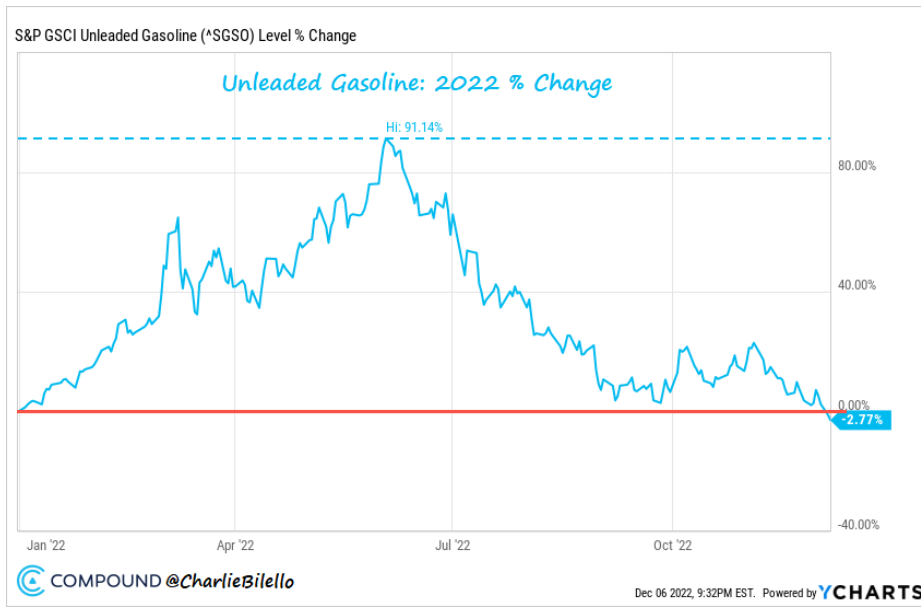
Country	Gross taxes	Capital spending	Production costs	Admin transport	Total
UK	0	22.67	17.36	4.30	44.33
Brazil	6.66	16.09	9.45	2.80	34.99
Nigeria	4.11	13.10	8.81	2.97	28.99
Venezuela	10.48	6.66	7.94	2.54	27.62
Canada	2.48	9.69	11.56	2.92	26.64
U.S. Shale	6.42	7.56	5.85	3.52	23.35
Norway	0.19	13.76	4.24	3.12	21.31
U.S. non-shale	5.03	7.70	5.15	3.11	20.99
Indonesia	1.55	7.65	6.87	3.63	19.71
Russia	8.44	5.10	2.98	2.69	19.21
Iraq	0.91	5.03	2.16	2.47	10.57
Iran	0	4.48	1.94	2.67	9.08
Saudi Arabia	0	3.50	3.00	2.49	8.98

Russian oil sales have also barely changed since their invasion of Ukraine:



Even if western nations have decreased their purchases of Russian oil, China, India, and other nations will happily fill that void. We do not think the reduction in energy prices has weakened Russia. This will have little impact on the invasion of Ukraine which seems more and more likely will become a long, stretched-out war.

Prices have dropped so much in recent months that retail gasoline is now down year to date.



The interesting part about this is market fundamentals in energy continue to get worse and energy prices continue to drop. The world reduced its supply of oil, increased its demand, and restricted a country from exporting oil to most advanced economies yet oil prices have dropped.

The Strategic Petroleum Reserves (SPR) are at their lowest level since 1984 and have been drained of 34% of their supply this year. China announced that it is reopening from Covid-19 this week. OPEC announced they will not change production levels last month even though the west has begged them to increase production. Russia announced they would not sell energy to countries that impose price caps on their product. Despite all these bullish signals oil reached another new level this week. Market fundamentals continue to improve for those that are long energy, yet prices continue to drop. We are not saying this week is a bottom but continue to point to the winter months where energy will be in extreme demand and shortages will more than likely occur across parts of Europe and potentially across the U.S.

Nothing has changed from our point of view. The recent price action has created new opportunities in names that got expensive in months past. The only thing that we know are the SPR will run out, the election is over, crude inventories continue to decrease, and price caps will be implemented on Russia, which is all bullish for energy assets - choose your assets accordingly. Remember, even in bullish environments in energy, there are major drops due to the volatility of the underlying commodities. We also remind you that every oil, gas, and coal-producing company will not be a winner in this cycle, choose accordingly.

MacNicol & Associates Asset Management
December 9, 2022