THE WEEKLY BEACON	MAY 19, 2023

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.

MacNicol & Associates Asset Management

Contact us today if you would like to meet about your investment future. *info@macnicolasset.com*

BEACONS OF THE WEEK

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.

Punta Santa Elena Light,
Salinas, Ecuador

Located in Punta Santa Elena, the westernmost point of mainland Ecuador. The lighthouse is located 3 kilometers west of the local yacht club. The present lighthouse was built in 1974.

Grotto Point Light, *New South Wales, Australia*

Grotto Point Light is an active lighthouse located at Grotto Point. The lighthouse was first lit in 1911 and is 19 meters high. It serves as the front range light, Rosherville Light serving as the rear light, into Port Jackson.

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

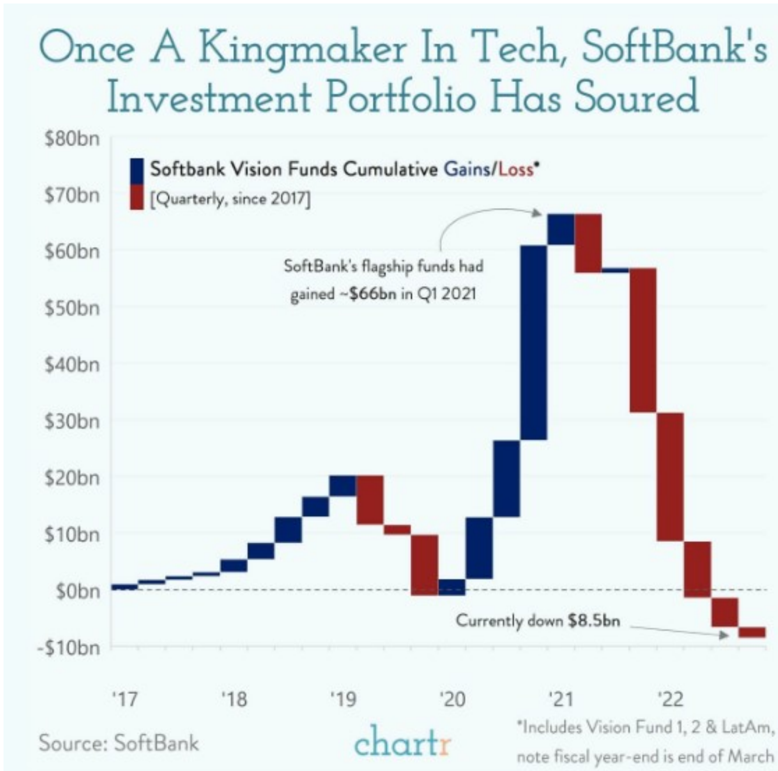
Softbank's bubble continues to burst

Softbank's Vision Fund reported a loss of $32 billion for the year ending March 31, 2023. The Japanese investing giant continues to suffer from valuation corrections and private markdowns across its private and public tech company portfolio. Softbank's poor performance this year contradicts the overall backdrop in the technology sector. Large-cap technology companies have rallied hard in 2023 erasing some of their 2022 losses. The reason Softbank's losses have ballooned is their investments are mainly in unprofitable, cash-burning tech companies that are speculative or have a long way to go before profit.

Softbank's roots go back to the 1980s but its place atop the tech sector roots back to a $45 billion investment from the Saudi Arabia investment fund in 2017, invested directly into the Vision Fund run by Masayoshi Son.

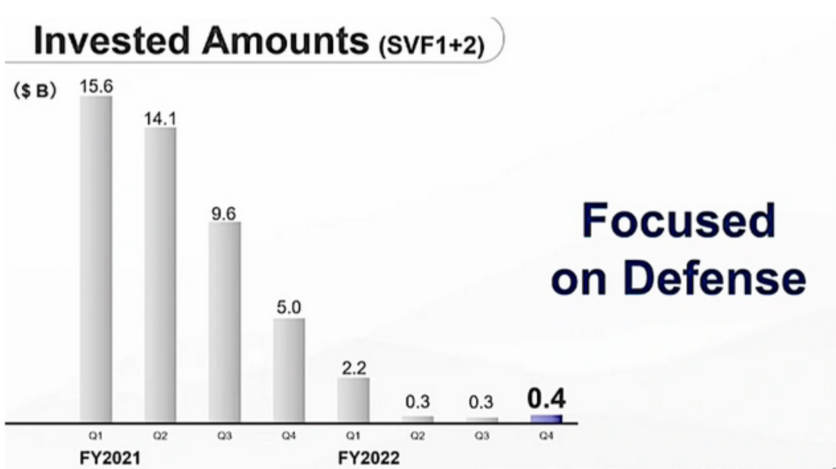
The Vision Fund was launched in 2017 with $100 billion in capital. The Vision Fund is the brainchild of Softbank's founder Masayoshi Son. The fund has invested in various technology companies including Uber, Door Dash, Nvidia, Slack, and many more. It is known as a large investor across private and public markets. Softbank was the investor originally responsible for grossly overvaluing WeWork and has lost billions in the process. Softbank was also an investor in FTX which went through their issues at the end of last year.

Softbank's Vision Fund had gained $66 billion by the end of the first quarter of 2021. Fast forward two years and the Vision Fund is now down, erasing all its gains.



Among the Vision Fund's losses this year, were an unrealized loss of $1.6 billion each in SenseTime Group and GoTo and nearly $800 million in DoorDash.

Due to large losses in the Vision Fund's portfolio, Softbank has slowed down its deal flow tremendously over the last year. Softbank has become very defensive in recent quarters, slowing down any new investments.

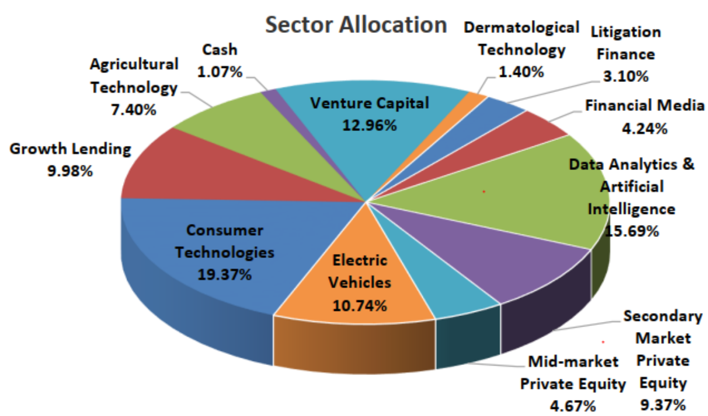


SoftBank said it made $3.14 billion in new or follow-on investments in its fiscal year, down from $44.26 billion in the same period of a year prior. A collapse in deals made by the Vision Fund is the result of tech valuations collapsing, limited capital, and volatility in markets. Who would have thought that investors would eventually care about valuations and cash flows?

Softbank has sold some of its remaining winners to cover its substantial losses over the last 18 months. Softbank and its investors are looking directly toward an IPO of British semiconductor firm Arm to help boost the firm's gains to the end of this year. Arm has filed the paperwork needed for an IPO in the U.S. The IPO of Arm will also give Softbank some liquidity for potential new investments moving forward.

This is yet another reminder of why valuations matter. The illiquidity of Softbank's private investments is also a reminder of the risks associated with Private Equity or Venture Capital versus investing in traditional equity. Most VC and Private Equity investors struggled in 2022 as technology valuations reset, liquidity dried up, and economic uncertainty arose.

Our Alternative Asset Trust has its private equity arm in which we invest in a portfolio of private companies. The MacNicol Emergence Fund began operations in 2010 and has invested in numerous companies across almost every sector. The MacNicol Emergence Fund was up 0.4% in 2022 significantly outperforming public equity markets and most private equity funds. The MacNicol Emergence Fund offers investors a diversified exposure to several sectors:

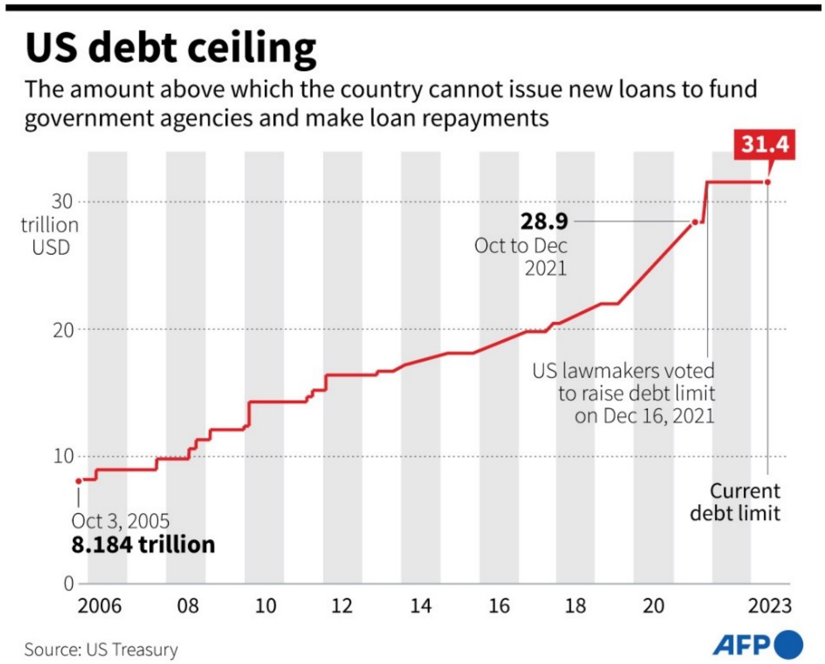


The Emergence Fund invests in private assets directly, and through limited partner funds.

Debt crisis winner

The impending debt crisis in the U.S. seems to be getting worse. For the U.S. government to continue its operations, Congress will need to agree on a Bill that will lift the debt ceiling yet again. Of course, President Biden and Democrats want a solution as soon as possible, as a government shutdown reflects poorly on them especially as we head into 2024's highly competitive election. The only problem is that they do not control the U.S. House of Representatives. The Democrats will need to barter with House Republicans to avoid a government shutdown. The United States most recently raised its debt ceiling in October 2021 when the debt ceiling was raised by $480 billion.

Almost every President over the last 40 years has raised the debt ceiling to drive their agenda.



We bring this up because the U.S. government could run out of money to pay its bills by June 1st according to Janet Yellen, Secretary of the Treasury. Running out of money/spending capacity would stop debt repayments, interest payments to bondholders, Social Security checks, and everything else the government spends money on. The debt ceiling not being raised could send the global economy into chaos.

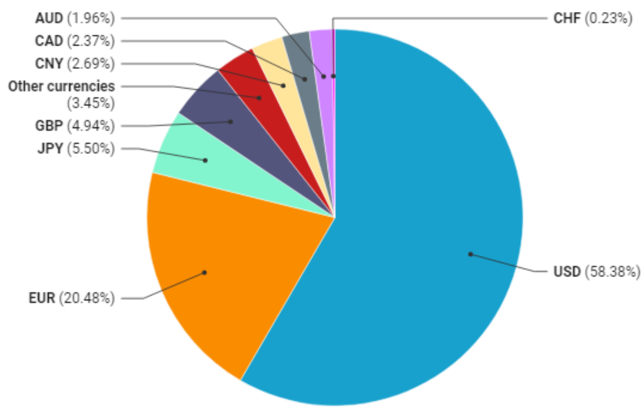
The potential default also gives Republicans the most power they have had in years as Democrats scramble to strike a deal. A deal between Republicans and Democrats would raise the debt ceiling and more than likely slow down government spending. Speaker Kevin McCarthy has repeatedly said that his party would raise the debt ceiling if Democrats and President Biden slash their spending moving forward.

As this crisis continues and the time to strike a deal shrinks, we wanted to highlight a major winner that would benefit from a temporary default by the U.S. government. (We do not think the U.S. will default and believe that both parties will more than likely agree on something to continue the government's operations. That deal will more than likely be agreed on at the stroke of midnight on June 1st.) However, if the U.S. does default, the real winner in financial markets could be our old friend gold. The store hold of value has performed very well this year despite Treasury Bills and Bonds paying a handsome interest rate. The U.S. government defaulting would send the U.S. Dollar in the wrong direction which would send investors and consumers to alternate store holds of value like gold.

The rise in the price of gold during a period of high-interest rates (2023) should send a warning to investors about the federal government's finances and the dollar's international status. The U.S. dollar has been the world's leading reserve currency since the Bretton Woods Agreement. That position could soon be in jeopardy as global Central Banks sell their U.S. dollar holdings. We are not saying a particular currency will replace the U.S. dollar as the leading global reserve currency but think a group of currencies may chip away at the U.S. dollar's dominance.

The U.S. dollar's share of global foreign exchange reserves has dropped from over 70% to 58% over the last 25 years according to the IMF. Despite this drop, the U.S. dollar still remains King with no other currency surpassing 21% of global reserves.

Foreign exchange reserves by currency, Q4 2022



Source: IMF COFER • Get the data • Created with Datawrapper

Geopolitical alliances and risks are major reasons that countries around the world are slowly dumping their U.S. dollar holdings and denominating trade in other currencies. These Central Banks are rotating into other developed currencies or precious metals. Central Banks added 228 metric tons of gold to their reserves in the first quarter of 2023. China has led the way in decreasing its U.S.-denoted holdings. Their U.S. Treasury holdings reached a 12-year low according to their most recent filings.

Could gold's recent performance also be a sign/warning of a coming debt storm? Or, is it the world decreasing its reliance on the U.S. dollar? We will wait and see.

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Traditional automakers making moves to grab market share

If you read this publication, you know our feelings on the electric vehicle industry:

- The industry will grow over the next decade, but mass adoption will not occur like the activists and green politicians claim
- Tesla will be a market leader (like they are today) and a few EV companies will chip away at that market share
- Traditional automakers we all know, and trust will also grab market share and will be Tesla's largest competitors
- Sourcing industrial and rare earth metals will be the key to increasing production
- Metal shortages could lead to higher prices which will slow the consumer adoption of EVs

Companies like Ford and General Motors have made serious head waves in the EV world and investors/analysts are taking note.

Ford has dived right in and is upgrading their production lines to construct EVs. They already have the space, technology, and people and are now upgrading their current production line to be able to produce EVs. Ford is also doing something very smart that will help them compete with Tesla. They are hiring former Tesla employees as well as former executives from mining and chemical companies. The employees they are hiring have the utmost experience and connections in these industries which will help Ford source raw materials which are in high demand.

Ford's executive director of advanced EV development, and chief advanced product development and technology officer, Alan Clarke, and Doug Field both worked at Tesla. Ford seems very serious about competing with the market leader.

Ford has locked up deals with lithium suppliers, Liontown Resources and Rio Tinto. Ford has also announced battery plants in Michigan, Kentucky, and Turkey.

Ford delivered 100,000 EVs in 2022 and hopes to make 600,000 in 2023 and eventually scale up to 2,000,000 by 2026.

Ford's numbers and profitability do not jump off the page in their current form. We are simply highlighting some of the moves the automaker has made in the last year to position itself as an EV market leader. No matter what you think, we are in the early innings for EVs. There will be money to be made throughout the process.

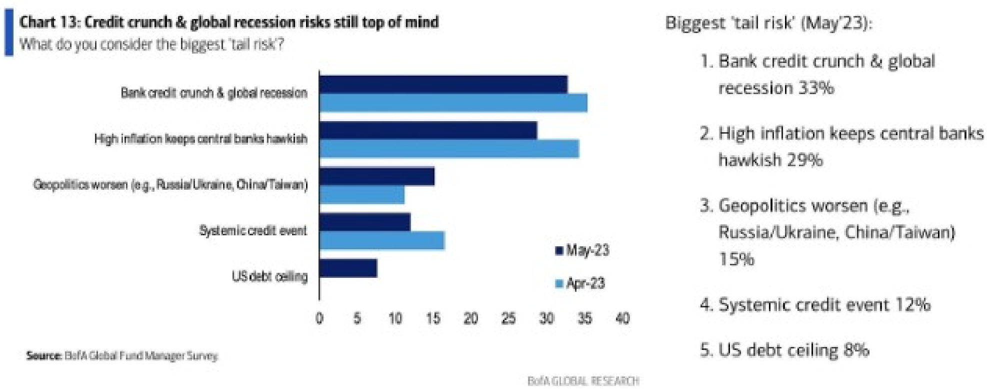
However, mass adoption and the scalability of the sector may take longer than many experts are claiming. Some experts believe there will be 350 million EVs on the road by the end of this decade, currently, there are only 15-16 million. The major variable that could help society reach this number is if EVs ever become less expensive than combustion engine automobiles. If a company created an EV that was cheaper than any other car, it would take over the market. The possibility of that seems unlikely due to the high input costs in EVs today.

Ford and GM were also huge winners from President Biden's EV goals as their EV models qualify for large tax credits.

Tail risk(s)?

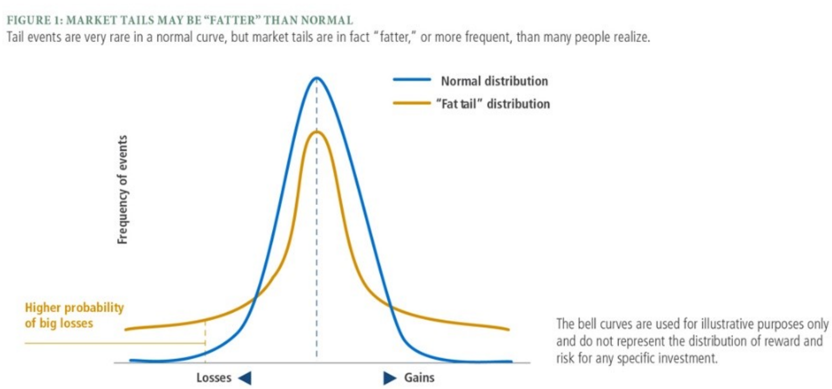
Bank of America conducted its most recent fund manager survey, and one response caught our attention.

Managers were asked what they see as the largest tail risk event moving forward.



Managers responded with the bank crisis as their biggest worry for a tail risk event.

For those of you that need a refresher on what tail risk is, tail risk is the chance of a loss occurring due to a rare event, in finance, this is the risk of an asset or portfolio moving more than three standard deviations from its current price.

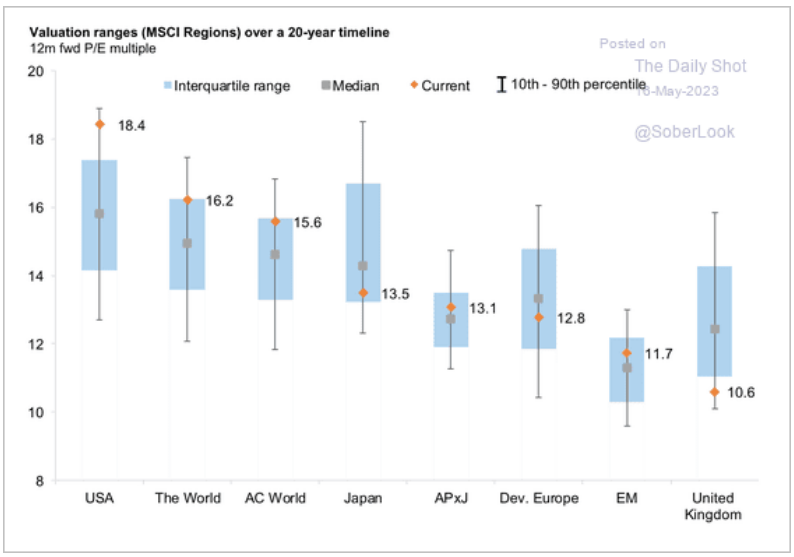


We are not surprised that fund managers are worried about the banking crisis but believed it would be more consensus as the number one issue. The other major responses include inflation remaining sticky, the war in Ukraine, other credit events, and the U.S. debt ceiling not being resolved.

However, a tail risk is usually something that has a very low probability of occurring. We think inflation staying high has a high probability. It is important as fund managers to map out every possible scenario moving forward to mitigate risk. It is also important to apply risk mitigation strategies in case one of these Black Swan or tail risk events occur. We are investors in a risk mitigation strategy that provides downside protection during "Black Swan" events. Contact us at info@macnicolasset.com if you have any more questions, we would be happy to answer them.

Expensive historically

U.S. equity valuations are close to their all-time highs. U.S. equities trade at a premium relative to global equities but they are trading even more expensively than they have over the last 20 years. Even global equities (The World) are trading at higher valuations than their 20-year averages.

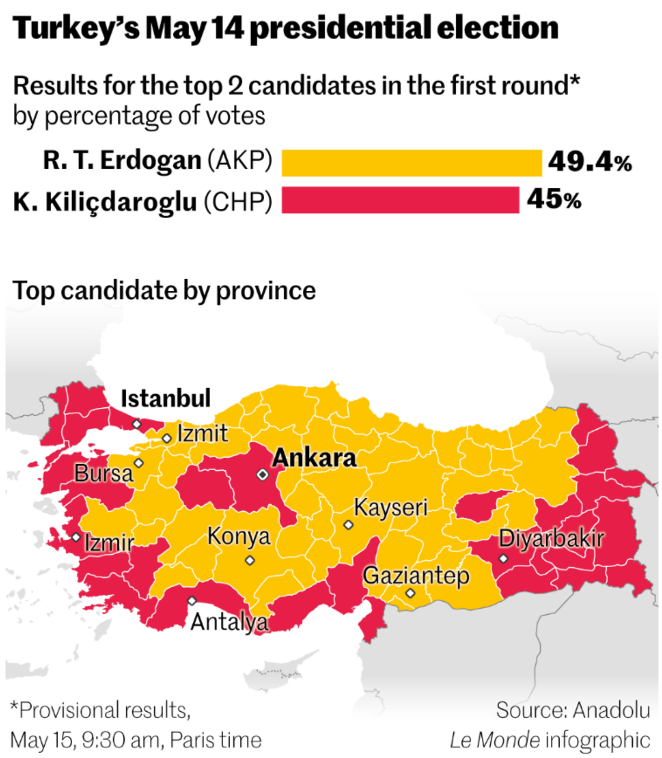


Are equity valuations remaining historically high due to falling hope from investors or optimism that earnings will grow?

We are not sure but think investors are holding on for dear life and are propping up the big boys (mega-caps) that are pushing the market in the right direction. Many U.S. technology companies are trading at massive premiums due to hype and hope rather than fundamentals. For now, it looks like British stocks are trading at the largest discount compared to 20-year averages.

Turkish election

Turkey held their presidential election on Sunday. Incumbent President Recep Erdoğan performed much better than polls expected, Erdoğan captured 49.4% of the votes which will send the country to vote again in a runoff election on May 28th.



Erdoğan has been the President of Turkey for two decades and if he wins in two weeks will clinch another 5-year term. The election will go to a runoff as no candidate reached 50% of the vote.

This uncertainty and Erdoğan's better than expected performance sunk the Turkish Lira to a new all-time low relative to the U.S. dollar.

The value of the currency cratered by more than 40% last year as Erdoğan's unorthodox economic policies fueled eye-watering levels of inflation.

The result also sent Turkish stocks in the wrong direction. Credit default swaps in Turkey surged 27% on this news to their highest level in 8 months. Many are surprised at this election result as Erdoğan had become quite unpopular in Turkey for his economic principles. While inflation began in 2021, Erdoğan directed the Turkish Central Bank to cut interest rates rather than raise them like the rest of the world. Fast forward a year and a half and prices are surging in Turkey. The CPI has increased by 43.7% over the last year.

Global Inflation Rates

Country/Region	CPI Inflation (YoY %)	Trend vs. Prior Reading
CHINA	0.7%	Lower
TAIWAN	2.4%	Unchanged
SWITZERLAND	2.6%	Lower
THAILAND	2.7%	Lower
SAUDI ARABIA	2.7%	Lower
JAPAN	3.2%	Lower
RUSSIA	3.5%	Lower
SOUTH KOREA	3.7%	Lower
SPAIN	4.1%	Higher
CANADA	4.3%	Lower
INDONESIA	4.3%	Lower
BRAZIL	4.7%	Lower
US	4.9%	Lower
NETHERLANDS	5.2%	Higher
SINGAPORE	5.5%	Lower
INDIA	5.7%	Lower
PORTUGAL	5.7%	Lower
FRANCE	5.9%	Higher
MEXICO	6.3%	Lower
PHILIPPINES	6.6%	Lower
NEW ZEALAND	6.7%	Lower
EUROZONE	7.0%	Higher
AUSTRALIA	7.0%	Lower
SOUTH AFRICA	7.1%	Higher
GERMANY	7.2%	Lower
IRELAND	7.7%	Lower
FINLAND	7.9%	Lower
ITALY	8.3%	Higher
UK	10.1%	Lower
SWEDEN	10.6%	Lower
POLAND	14.7%	Lower
TURKEY	43.7%	Lower
ARGENTINA	104%	Higher
VENEZUELA	471%	Lower

CREATIVE PLANNING @CharlieBilello

Moody's released a note to readers last week that an opposition victory would bring optimism and potential stability to the Turkish economy while an incumbent victory would be negative to the Turkish economy and could result in a currency crisis.

Turkey is a G20 country that is a member of NATO. Western nations often rely on Turkey as a middle eastern ally and as a major trade route. Turkey is home to 84 million people (the 17th largest population in the world) and is the world's 19th largest economy (real GDP). Turkey defaulting or continuing to struggle is not a random developing nation having economic difficulties but it's a world power on the brink of a currency crisis and potential default.

The one thing the Turkish population may like about Erdoğan and his policies is their retirement portfolio returns. While equity and debt markets around the world were blown out of the water in 2022, Turkish equities surged. The iShares MSCI Turkey ETF was up 106.42% in 2022 (no that is not a typo).

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The ETF is down 18% in 2023. Turkish equities are extremely volatile and are quite unpredictable to forecast due to the unpredictability of the government and the Central Bank.

Economists believe the Turkish government has spent $177 billion since December 2021 to support the sinking Lira. Turkey is currently deprived of foreign capital even though it is a major economy due to it being unpredictable and not trustworthy.

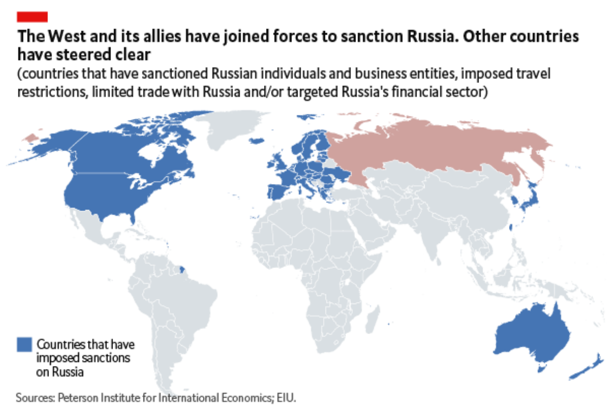
This could make Turkey ripe for the taking from the West. We have reported in previous issues that Turkey is making decisions that benefit itself and not the West. It has recently made moves that have angered the West and favored eastern nations like China and Russia. We think Turkey will continue to play this game moving forward and will not allow the West to bully them like they have in decades past.

Turkey's refusal to go along with sanctions on Russia and its transformation into a Russian 'transit hub'

25.10.2022

> Answer in writing

The one gap between this map:



And this map:

Is Turkey.

Ole Faithful's status

We ran by a great image and study this past week. The study is from TheMacroCompass.com and looks at the 60/40 portfolio. The portfolio strategy investment advisors have been utilizing for decades for their clients gave clients a balanced approach to their retirement with equity and fixed income allocation. The fixed income allocation was historically supposed to perform well while equities underperformed allowing investors to at worse break even (in very down years for the stock market).

The strategy did its job for decades but eventually stopped working.

During the Financial Crisis, something happened, and the fixed income portion of a 60/40 portfolio could not make up for the shortfall that equities produced in that period. Yields got low enough that they could not produce enough torque for a 60/40 portfolio to do its job. In 2022, bonds had their worst performance in decades due to rising interest rates. The balanced portfolio was blown out of the water and investors finally seemed to realize that this strategy is flawed.

The major flaw in the strategy is it does not consider all macroeconomic environments and it is a static strategy from a holistic point of view. The group at TheMacroCompass.com went back to 1880 and calculated the real returns of a 60/40 portfolio by decade:

The 60/40 portfolio doesn't fit all macro regimes

Decade	Total Return	Inflation	Real Total Return
1880 - 1889	6.0%	-2.2%	8.2%
1890 - 1899	5.7%	0.1%	5.6%
1900 - 1909	10.2%	2.4%	7.8%
1910 - 1919	4.5%	6.6%	-2.1%
1920 -1929	15.2%	-0.9%	16.1%
1930 - 1939	0.1%	-2.0%	2.1%
1940 - 1949	8.9%	5.4%	3.5%
1950 - 1959	19.3%	2.2%	17.1%
1960 - 1969	7.7%	2.5%	5.2%
1970 - 1979	5.7%	7.4%	-1.7%
1980 - 1989	17.4%	5.1%	12.3%
1990 - 1999	18.1%	2.9%	15.2%
2000 - 2009	-1.0%	2.5%	-3.5%
2010 - 2019	13.4%	1.8%	11.6%

Source: TheMacroCompass.com

In 3 of the last 4 decades, the 60/40 portfolio shot the lights out, just like indexing. Those periods all had the same macroeconomic backdrop, low growth, declining interest rates and low inflation.

The study also calculated that the annualized volatility of a 60/40 portfolio was approximately 14% over the last 100 years which seems quite low. However, there have been 8 instances in the last 100 years (including 2022) where 20-70% of a 60/40 portfolio has been wiped out. This drawdown could seriously impact financial decisions for consumers especially those closing in on retirement.

Unless you think the rest of the 2020s will be like the last decade and the 1990s (low inflation, and low growth), the 60/40 portfolio will more than likely not perform well.

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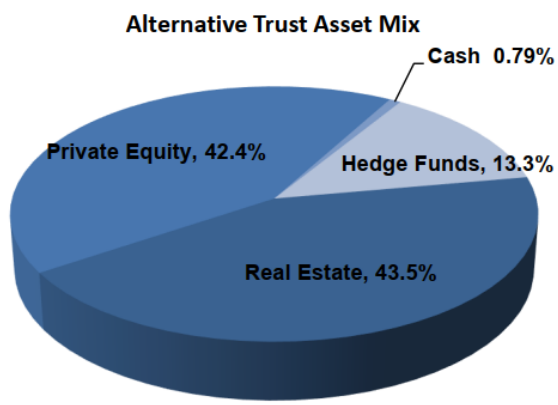
Other asset classes like global equities, precious metals, and alternative assets can help construct a truly diversified portfolio that is prepared for any type of macroeconomic environment. The failure of the 60/40 portfolio was one of the major reasons MacNicol & Associates Asset Management launched its Alternative Asset Trust which opened in 2010. The Alternative Asset Trust has audited results and has produced an annual return of 10% (net of ALL fees and costs) and annual volatility of 6.8% since inception. This is something we are VERY PROUD of. You would have to go back to the 1980's and 1990's to find low annual volatility like this. We look forward.

The Alternative Asset Trust has a diversified exposure to various asset classes:



*As of March 31, 2023

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May 19, 2023

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