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 our 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.

Castillo Grande Light, Cartagena, Columbia

This lighthouse was built in 1973. The lighthouse stands at 79 feet tall. The lighthouse marks the entrance to the main harbour at Cartagena and sits on property owned by the Columbian navy.

Cap-au-Saumon Lighthouse, Saint-Siméon, La Malbaie, Quebec

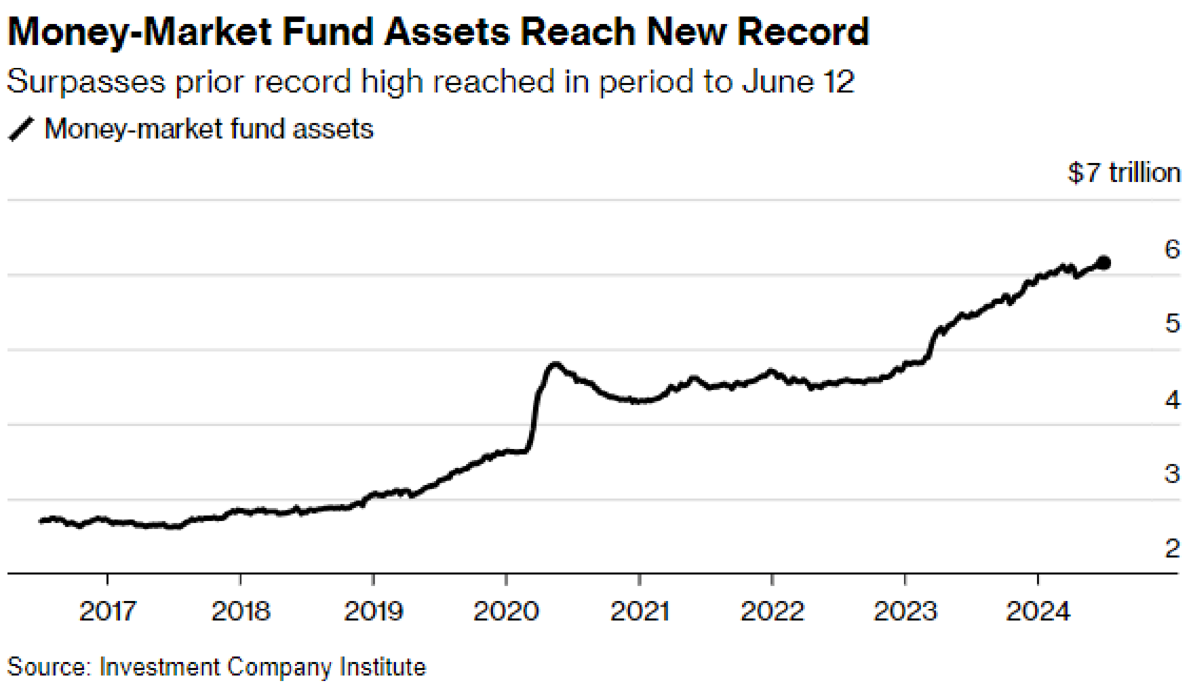
This lighthouse is a lighthouse on the St Lawrence River that was commissioned in 1894. The lighthouse stands at 46 feet tall. Currently the lighthouse is rented by the week and is a recognized heritage site.

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

Investor uncertainty

Despite markets hitting new all-time highs every week, investors continue to pour record amounts into money market funds.

According to the Investment Company Institute, money market fund assets hit a fresh all-time high last month. Assets in the asset class surpassed $6 trillion earlier this year, more than double the amount at the start of 2019.



The amount of money pouring into money market funds is perhaps a sign that investors are worried about the state of markets and the global economy. Over the last 2 years valuations have been severely stretched while the economy has seemingly slowed across the developed world.

We believe some companies and industries have an upside from here across equity markets. However, for those who have reaped the rewards of indexing over the last decade and a half, perhaps now is the time to diversify and park their money across several strategies including global value and money market funds.

Our investors know that we have utilized money market funds as a cash proxy as yields have risen over the last 18 months. However, our exposure to the asset class for the most part is capped at just a few percent so that we can be tactical for opportunities that present themselves.

Moving forward, where do you see the amount of money in money market funds going? Do you see it increasing or decreasing over the next 6-12 months?

September surprise

As we get closer and closer to the election, it will be interesting to see if the FED decides to make an interest rate policy change and impact the decision of voters. The FED is supposed to be nonpartisan and is not to be influenced by the government.

We are in the camp that an interest rate change in July or September would not impact our vote. It has been four years and your decision should be based on more than a 25-basis point decrease in the FED Funds rate a month before the election.

We bring this all up this week because the probability of an interest rate cut at September's FED meeting (the last FED meeting before the U.S. Presidential Election) has increased over the last few weeks quite substantially. Currently, there is a 77% probability that rates will be lower in September, a month ago that number was 51%. So, what has happened?

Some economic numbers are breaking down across the U.S. and economists think the FED will bail out consumers before we get a recession. Investors want to speak interest rate cuts into existence so that they can lower their terminal rate in their financial models and get even more bullish on equities.

However, we think this spike in the probability of a cut at September's meeting will be short-lived and will decrease in the coming weeks. We think eventually there will be no interest rate cut until after the election. Perhaps, we are being a bit naïve in our thinking. We also think the FED will continue to drag its feet in decreasing rates as the annual inflation rate remains elevated and perhaps accelerates slightly through this summer.

Before you slam us for being a pessimist you must remember that since last October's FED meeting, FED Funds futures have been pointing to rate cuts at basically every meeting at one point before reversing. We think the market has been extremely excited for rate cuts basically since rates have moved upwards. We think some commentators and investors are even trying to talk rate cuts into existence.

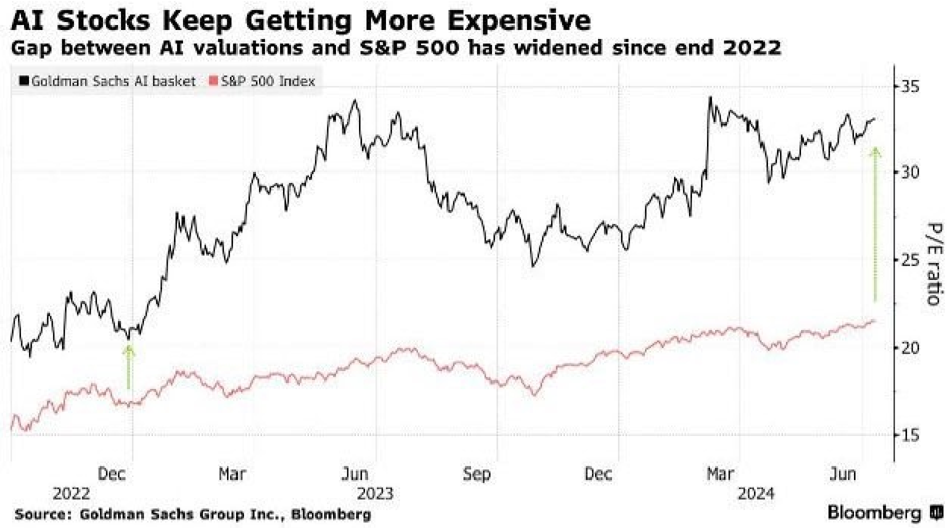
We think that eventually there will be rate cuts but believe that rates will continue to be higher for longer moving forward.

And just two hours after we wrote about this, Chairman Powell spoke in front of the Senate Banking Committee and said that first-quarter data does not support the greater confidence in the inflation path the FED needs to cut rates.

Artificial valuations

As markets continue to melt up, valuations continue to stretch. However, one part of the market is much more expensive than the rest of the market. If you guessed technology is the pricey area of the market that we are talking about, you would be partially correct. We are talking about the sub-industry of artificial intelligence.

Goldman Sachs tracks a basket of AI stocks as well as metrics for said basket. According to data from Goldman and Bloomberg, the AI basket is trading at a P/E ratio of over 32x while the S&P 500 trades below 22x earnings.



There is going to be a spread between the valuations of AI stocks and the rest of the market. AI stocks will have higher earnings growth rates moving forward and justify higher valuations. However, we wanted to talk about how the trend in the chart above has changed in a matter of 18-20 months. Look at the P/E ratios for both indices back in December 2022, the spread is quite thin and then explodes through 2023 purely from the AI basket getting much more expensive. AI stocks were the strongest performers in 2023 and their performance increased their P/E ratios quite substantially. We are here to ask a simple question. Is this outperformance sustainable in the long run and are these valuations justified?

We know every investor uses their models and reads coverage from analysts they prefer; we just think this trend might be overdone and the outperformance by this basket could slow down. That does not mean AI stocks will tank 25%, it purely means their outperformance could disappear and other areas of the market could play catch up and trim the spread that has been created over the last 18 months. We are not questioning AI and its applications; we know AI will play an integral role in the future but believe the recent trend might be a bit overdone.

Legend of the buyside pokes at Tesla

Legendary investor Bill Gross put out a statement on X this week that surprised many. The former CIO and Founder of Pimco said that Tesla is acting like a meme stock – sagging fundamentals, straight-up price action, and pumping.

The irony of his post on X is Elon Musk owns both Tesla and X.

Gross's post came after Tesla shares moved up 44% over 10 business days after strong vehicle deliveries and production data were released which beat analyst expectations.

Gross went on to compare Tesla to Chewy, Zapp, and even GameStop. Gross has previously revealed that he dabbled in trading GameStop and AMC in 2022 calling the options he bought "lottery ticket stocks".

Gross pointed to deliveries being down year over year by 6% which many investors probably did not even know as the headlines have read "beat analyst expectations".

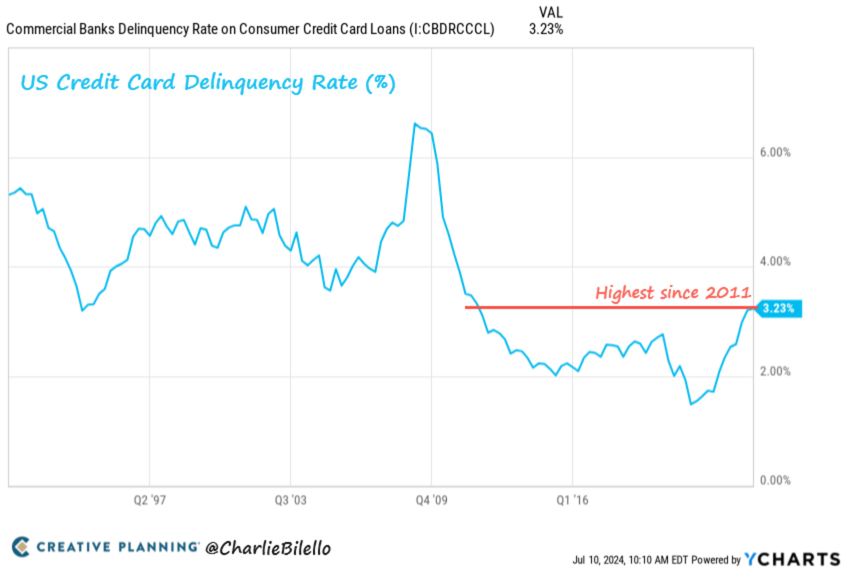
This is not the first time Gross told investors to avoid high-growth stocks this year. He recommended avoiding the tech sector to start this year and recommended buying value and energy infrastructure stocks.

We are not buying Tesla shares at current valuations unless their self-driving taxis launch sometime soon. Tesla is hosting an event on August 8th for its potential robotaxi business unit which many along with us are watching quite closely. Tesla's market share has shrunk in recent quarters as competition ramps up across the electric vehicle industry. In fact, on Wednesday data provider Cox Automotive reported that Tesla's U.S. market share slipped below 50% for the first time since it launched its first EV.

Tesla is also facing issues that are plaguing the entire EV industry. Consumers have recently shown they are not as willing to make the switch to an EV as many once believed. The main obstacles for EV producers from a consumer standpoint are price and reliability.

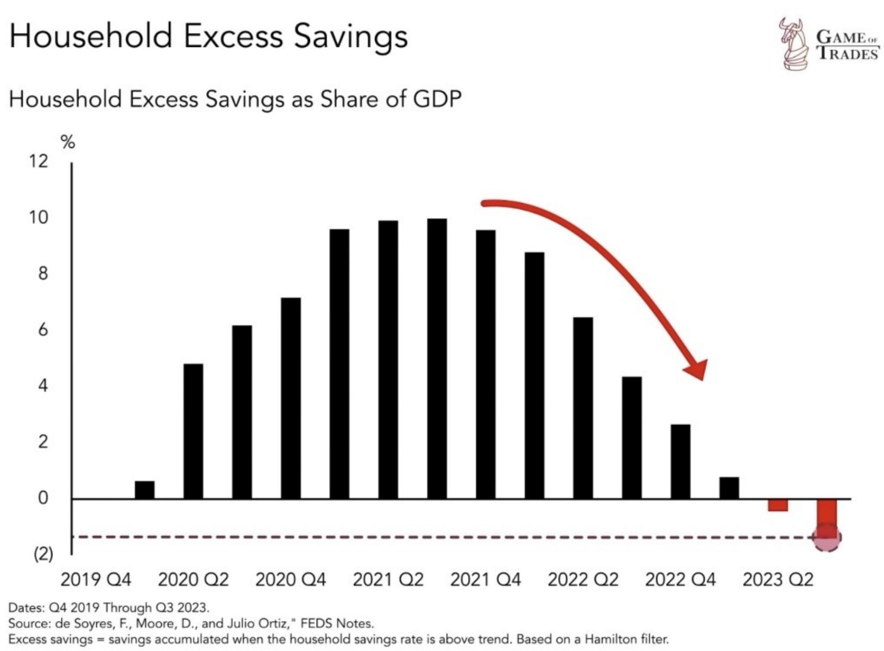
Consumer balance sheets breaking down

Consumers are struggling. Full stop. Rising rates, numerous years of elevated inflation, and dwindling savings accounts have led consumers to pile on credit card debt. According to Charlie Bilelo that debt for consumers has added up. Credit card delinquencies in the U.S. have reached their highest point since 2011.



Delinquencies have surged over the last 2-3 years. At the same time, interest rates on credit cards have increased. Consumers are taking a page from the government's playbook and buying stuff that they cannot afford.

So why has that happened? What happened to all the excess savings that consumers piled on during COVID-19? They spent it.



Excess savings for consumers reached $2.1 trillion in 2021 while the economy was shut down. Government stimulus and the inability to do things during Covid-19 lockdowns led to this phenomenon. However, consumers have since spent all this excess savings as we have exited COVID-19 and are now running dry on savings. Despite this lack of savings, consumers want to continue to live like they were and are spending more than they can afford.

According to WalletHub, 46% of Americans are paying off credit card debt from last summer. The average credit card interest rate has increased from 14.5% in May 2020 to 21.5% in May 2024. Servicing debt has become more expensive than ever in the 2000s.

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More gold

Are you following along?

Global Central Banks continue to buy gold and sell U.S. Treasuries.

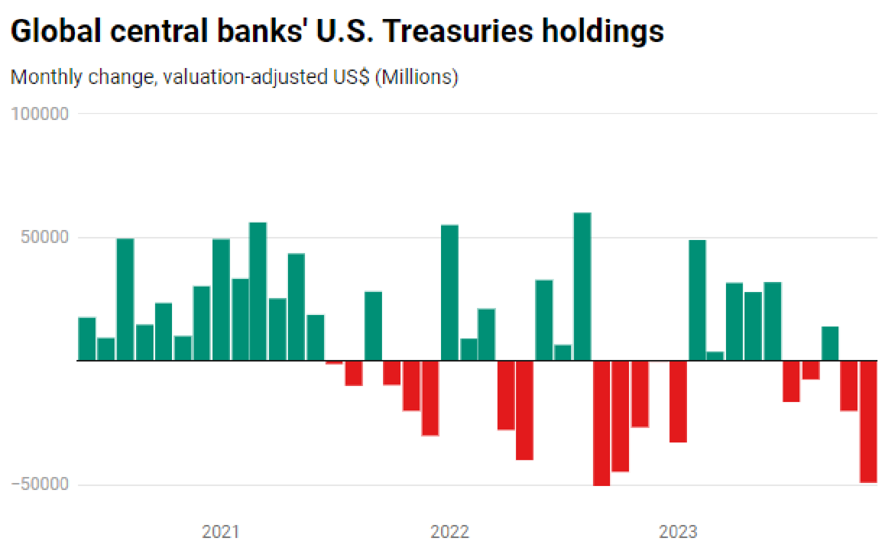


Chart: Jamie McGeever • Source: U.S. Treasury, Federal Reserve • Get the data • Created with Datawrapper

Central Banks are even moving their gold reserves onshore in a move that mitigates potential risk factors down the road. Last week India moved 100 tons of gold that were held in the UK to domestic vaults. The country has also boosted its Central Bank's gold reserves by the most in 2 years.

Central Bank gold purchases have been a major driver of gold's price performance this year. Central Banks have piled into the physical metal as geopolitical risks have heightened, trade wars have ramped up, and the global economic landscape has worsened. China, India, and Turkey's Central Banks have been major buyers of gold in recent years as the countries have cut their U.S. Treasury holdings.

Even European countries have piled into the precious metal in preparation for harder times fueled by uncertainty. Serbia's leader said that his country plans to buy gold with every dollar of surplus money moving forward. What does that tell you?

Serbia Boosts Gold Reserves to Prepare for 'Hard Times': Vucic

By Misha Savic

(Bloomberg) -- Serbia's central bank bought 5 tons of gold last week for €350m to enhance "financial security" of the country, President Aleksandar Vucic says in live interview to Belgrade-based Pink television.

- Total gold reserves now at 46.5 tons and "we're yet to buy gold with every surplus of money that we will have:" Vucic
- "We want to be safe and secure in hard times, which I expect as the president of the republic:" Vucic

With all of these buyers, demand continues to grow. Prices will follow as there is no alternative for gold.

It's also worth noting that mainstream media outlets and some analysts are waking up to gold. Just a day after Jerome Powell spoke about inflation at a Senate hearing, CNBC posted the article below talking about why gold jumped on Wednesday morning.

CNBC MARKETS BUSINESS INVESTING TECH POLITICS CNBC TV INVESTING CLUB PRO

Gold ticks up on Powell's comments; U.S. inflation report awaited

PUBLISHED TUE, JUL 9 2024-11:33 PM EDT | UPDATED 3 HOURS AGO

REUTERS

WATCH LIVE

Gold traded in a narrow price range on Wednesday as investors looked forward to a key U.S. inflation reading that could shed more light on the Federal Reserve's interest rates trajectory.

Alexander Manzyuk | Anadolu Agency | Getty Images

Gold prices edged up on Wednesday, a day after Federal Reserve Chair Jerome Powell's comments suggested the case for interest rates cuts is getting stronger, while investors braced themselves for a crucial U.S. inflation report.

We think we are still in the early innings of a multiyear run for gold and are positioned accordingly with physical exposure, as well as both junior and senior gold miner exposure.

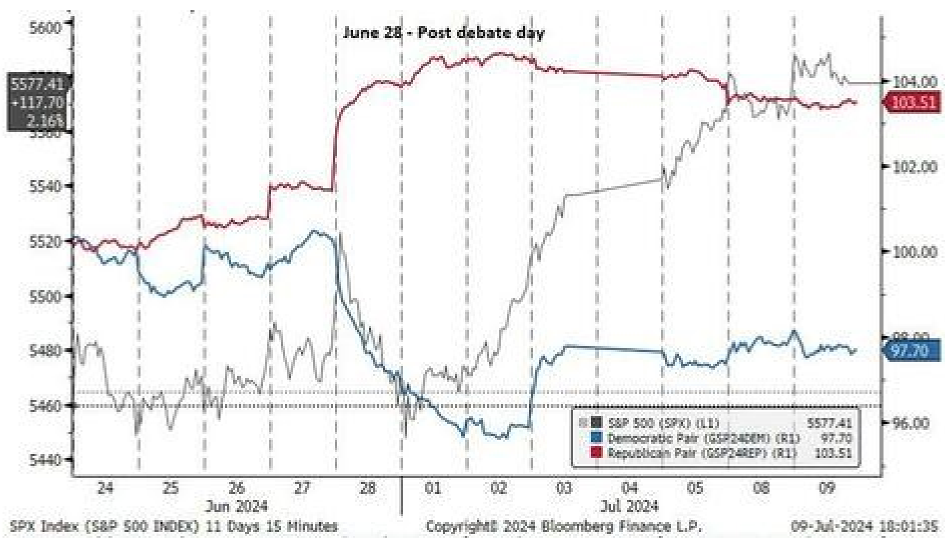
*Disclaimer: MacNicol & Associates Asset Management owns various securities involved in the gold industry including physical gold, gold ETFs, and gold mining companies. **

What the market is pricing in for November

According to Goldman Sachs, the market is pricing in a Trump victory in November paired with a Republican sweep in the Senate and House.

If you have followed the news over the last week or two, this comes as no surprise. Biden's debate performance was very poor, and it has caused many Americans including politicians in his party to doubt his health and ability to win. The media has even turned on him.

Goldman's thematic trader Louis Miller says the moves in the market that his team has seen since the debate in late June were similar to the moves that we saw across markets in 2016 after Donald Trump debated Hilary Clinton.



Source: *Goldman Sachs FICC & Equities, Bloomberg, as of 10-July-2024. Past performance is not indicative of forward returns.*

According to Miller investors are positioning themselves for a Trump victory and a republican sweep. The poorest performers after the debate were industries that could face challenges with Republican-implemented policies. These industries include Battery Storage, Clean electricity, and EVs.

We are not going to tell our readers how to vote or what we believe. We are nonpolitical. However, we must follow the election and position ourselves accordingly as it's our responsibility to follow major events like the elections as a fiduciary for our investors.

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