THE WEEKLY BEACON	January 31 2025

This commentary was written by our team and NOT outsourced to a third party. 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.

Buffalo Main Lighthouse, Buffalo, New York

This lighthouse is located in Western New York, beaconing around Fort Niagara. Congress allocated $17,000 in March of 1817 for the construction of this lighthouse along with another in the region.

Charlotte–Genesee Lighthouse, Rochester, New York

This lighthouse is an 1822 lighthouse shaped as an octagon. The 40 foot lighthouse is located on Lake Ontario. In 1881, the lighthouse was turned off, the lighthouse then was moved to a pier in 1884 after the shoreline in the area was altered.

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

A Monday surprise

If you woke up on Monday, market action probably caught you off guard. Nasdaq-100 futures were down over 4%, driven by an 11% pre-market drop from Nvidia. The entire technology and AI world tanked on Monday due to a massive technological development by a Chinese company.

A Chinese AI service provider which is a startup has seemingly upended the AI market and has put providers like Nvidia, Microsoft, and ASML on notice. DeepSeek is a Chinese-based AI lab that develops open-source language models. DeepSeek's controlling shareholder is Liang Wenfeng, co-founder of quantitative hedge fund High-Flyer, based on Chinese corporate records.

The Chinese start-up launched its free assistant on the App Store on January 20th and the program reportedly can compete with OpenAI's Chat GPT. What has the entire technology world on notice is its popularity has grown exponentially; the company has made the program open source and its costs are much less than the AI models/platforms developed by other competitors in the industry. DeepSeek's company has upended the industry assumption that AI requires huge investment and the companies that will lead the innovation are the largest U.S. companies that have the technology and capital to invest and innovate AI technologies.

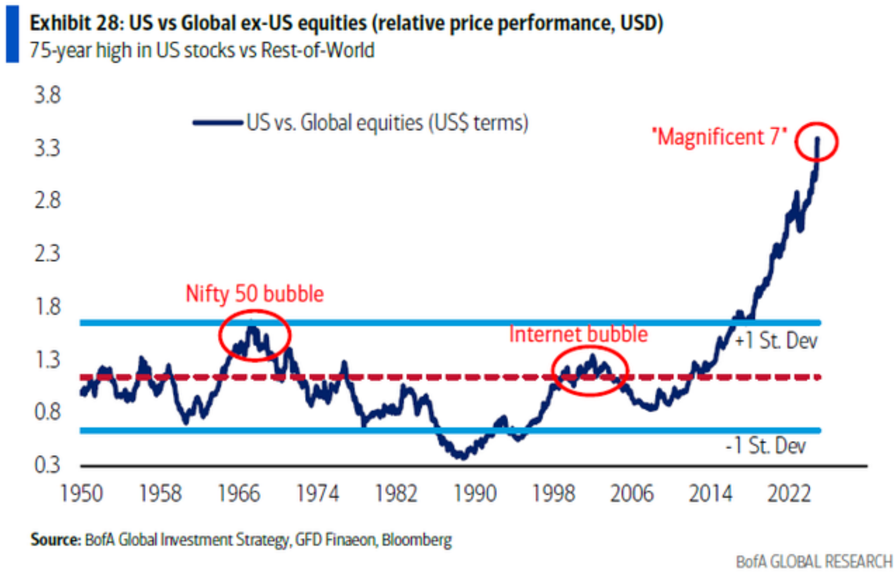
The development over the last week has led DeepSeek's program to rise into the number one position on Apple's App Store. It also led to the stocks of chip makers like Nvidia, energy providers, and other AI market participants dropping sharply. This development out of China could upend the AI industry and destroy Nvidia's dominant market share, which has led it to become the world's largest company (in terms of market cap).

On the cost front, DeepSeek published a paper earlier this month where they claimed their DeepSeek V3 cost less than $6 million worth of computing power from Nvidia H800 chips. Last year, Microsoft and Meta bought a combined 800,000 chips, this breakthrough could be devastating for chip makers like Nvidia.

Venture capitalist Marc Andreessen who is a technology advisor to President Trump compared this Chinese innovation to the Russian launch of the first artificial Earth satellite.

Although futures bounced back slightly, the AI trade has suffered a blow. This blow comes at a very critical point as numerous tech companies are due to report earnings this week. Microsoft, Tesla, and Meta Platforms are due to report on Wednesday, and Apple and Amazon are due to report on Thursday.

Coincidentally, 324 of the 500 S&P 500 components opened higher on Monday. This market shock truly only heavily impacted the beneficiaries of AI. These U.S. technology providers have had quite a run and have dominated markets for quite some time. Is now the time to sell them as they see their dominance slipping away? U.S. equities are at a 75-year high versus global equities in terms of relative price performance.



We will finish with a few thoughts. Some industry analysts are questioning how real the numbers that DeepSeek reported are. DeepSeek did not include prior research and development costs related to the development of the program. We do not blame these analysts for their doubts, after the last few years why would anybody from the West trust China, and even if this program is real, how many Western people would trust using this platform? We certainly would have major questions.

We think yesterday's market reaction may have been overdone. The overall energy demand is not going anywhere due to a potential technological breakthrough. Uranium stocks are now as attractive as they have been in quite some time. The same goes for some energy providers that pulled back heavily on Monday. We hope you were looking for opportunities. We know we were. This is not structural at least in terms of the companies that we own. We think it's simply selling pressure that accelerated due to losses from a few big names, like Nvidia. We will continue to monitor the situation and will report back soon.

On Tuesday, the U.S. government along with Microsoft and OpenAI were reportedly investigating China and DeepSeek where there are rumblings that DeepSeek ripped off ChatGPT. OpenAI CEO Sam Altman accused DeepSeek of intellectual property theft. Trump's AI czar echoed similar concerns.

We are not sure on the validity of these comments as its early but would not put it past China.

Home prices gaining steam

Home prices across the U.S. rose at an annual rate of 3.8% as of November. This jump comes despite mortgage rates rising over the last few months. November's jump topped the previous month and was predominantly driven by the largest 20 metropolitan areas where home prices jumped 4.3% over the same period.

The lagging data confirms that consumers were not spooked by rising mortgage rates.

The median previously owned home sold for $404,400 in both November and December, according to the National Association of Realtors—up 4.3% and 6% from the year prior.

Housing costs have dominated headlines over the last year or so as inflation rates remain elevated. Demand continues to remain robust. Prices remain elevated due to a lack of movement from consumers who locked in mortgages during 2020 and 2021.

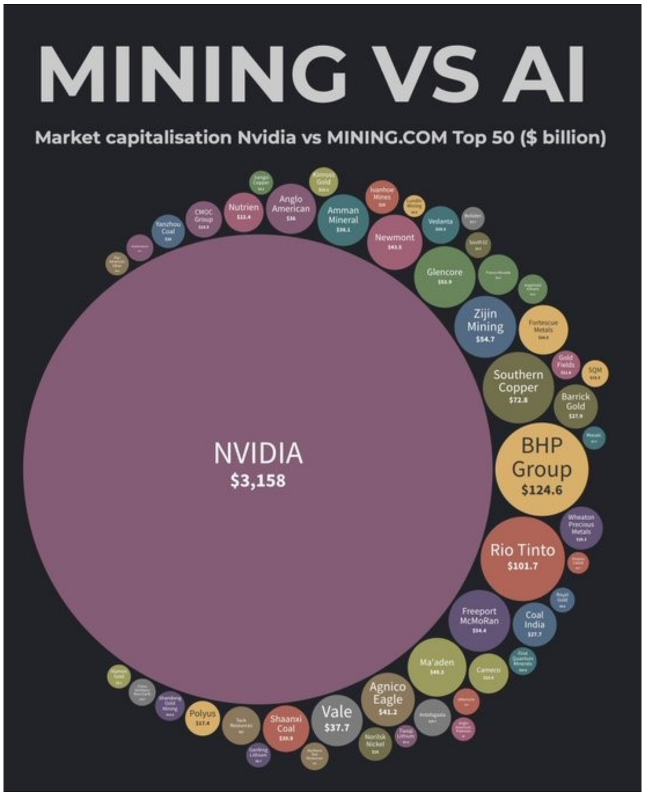
According to numerous industry forecasts, prices are expected to rise yet again in 2025, although at a slower speed than we have seen in recent years. The Mortgage Bankers Association sees prices rising by at least 1.5% while Fannie May is forecasting a 3.5% price jump. Mortgage rates remain above 7% and industry experts do not expect much relief in terms of lower rates this year.

On a positive note, incomes are forecasted to grow at a faster rate than home prices which will benefit many homebuyers.

One key data point that many overlooked is the price movement of homes in the Northeast. The area was left for dead when millions of Americans moved south in the early days of Covid-19. However, last year prices in the Northeast jumped 11.8% according to data from Realtors Group. A lack of new inventory is the predominated driver of this trend.

Mining upside

A picture is worth 1,000 words. This is not a saying we came up with but it does a great job of describing the image below.



Talk about relative value. Miners produce tangible products needed across various industries. They also produce products that hedge inflation. The run that Nvidia has gone on in recent years has been historic, but we expect some value names including a few miners to play a bit of catch-up moving forward.

Here are the largest 5 mining companies by market capitalization in the world.

Company	Country	Market Cap
BHP Group	Australia	$180 billion
China Shenhua Energy	China	$151 billion
Rio Tinto	UK	$143 billion
Southern Copper	USA	$105 billion
Zijin Mining	China	$83 billion

Their collective market capitalization is approximately $650 billion. Nvidia lost over $600 billion in market capitalization this past Monday.

Just looking at the gold industry, gold miners are extremely undervalued for where the price of gold has been trading. If you want to talk about strong earnings and cash flows, look no further.

Currently, we predominantly own precious metal producers across the mining space. Our holdings predominantly trade at nice multiples and include mostly large names that industry experts are familiar with. We also own a few small cap names for some growth potential as they

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1. Trade inexpensively
2. Have upside potential and
3. Some quality small caps are nice acquisition targets for majors.

We have been more bullish on precious metal miners relative to industrial miners over the last year or so due to the upside and inflation protection. We like gold, and silver as inflation hedges over industrial metals and we also saw some economic weakness which slowed the demand for industrial metals. This weakness that we describe was most prevalent in China, the largest manufacturing country in the world.

Disclaimer: MacNicol & Associates Asset Management holds various precious metal miners across various client accounts.

S&P 500 short interest at decade low

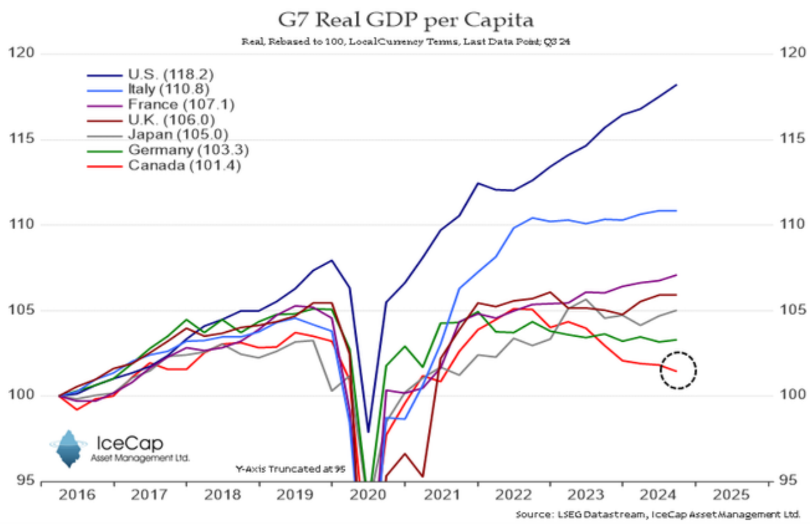
Short sellers have seemingly thrown in the towel according to Bloomberg and Macrobond. Short interest on the SPDR S&P 500 ETF Trust, a proxy for the overall index is at an all-time low. The data series dates to 2011 and tracks the number of shares held short against the ETF. Since early 2020 the number of shares held short against the ETF has been more than cut in half.

Short sellers are facing margin call after margin call. Their investors are growing tired of the negative results. The ironic part of this phenomenon is the index is relatively expensive, the economy is weak, and inflation has surged. Comparing this market environment with the past it made sense to short, however, the market is not acting rationally, and it seems the economy and stock market's correlation is decreasing.

Short-selling funds have even been forced to shut down shop as markets continue to melt up despite it being historically expensive. Last week, Hindenburg Research, a popular activist short seller which we have mentioned in this publication in the past closed shop. The founder gave no reason for closing his firm, but it highlights the wear and tear of the industry. According to Breakout Point, there are only 42 active short-seller firms, down from 66 in 2019. These short sellers do not use shorting like traditional hedge funds. These pure short sellers are betting against companies, countries, or indices for whatever reasons. We know funds like these do not short the S&P 500, however, the 2 different data points highlight a trend. An overall trend that illustrates the art of short-selling dying (at least for now).

A Canadian lost decade

This chart we are about to share hits close to home. As a Canadian firm, we have deep roots across our country. The chart below illustrates how tough Canadians have had it over the last decade. The chart tracks GDP per capita over the last 10 years.



Canada's growth has been almost nonexistent over the last 10 years, and it has the worst growth amongst its G7 peers. Truly remarkable how many failed policies has decreased productivity and increased regulation across Canada. We hope as a country we can get back on track but for now, it seems we are experiencing a cycle more correlated with Western Europe than our neighbor the U.S. You may think Europe is innovative with their German cars, and French nuclear energy and it is a beautiful place to be compared to. However, we will warn you that Western Europe is forecasted to have the slowest growth among major economies moving forward. Capital is rotating out of the area and into more attractive regions. We truly as Canadians hope we can get back on track through new policy and less red tape. Until that happens capital both financial and human will continue to leave our country.

Jerome and the FED

The U.S. Federal Reserve made its first policy decision under President Trump's second presidency on Wednesday. Trump has been very critical of Powell in recent months claiming that rates should be lower, and the FED should not be a thing.

On Wednesday, the FED announced they would be holding the federal funds rate in place, a move that surprised nobody. It has been a consensus for a few months now that at January's meeting, the FED will stop cutting for now. Economists have pointed to a potential second wave of inflation as a reason for the pause. The Federal Open Market Committee (FOMC) voted unanimously to keep rates in place.

Powell's description of inflation changed since the FOMC's last meeting. In December, he mentioned progress on slowing price growth. This month he mentioned progress on inflation but it continues to remain elevated.

Powell said the FOMC needs real progress on inflation or a weak job market in order to cut interest rates moving forward. However, he also stated that the FED does not need to wait for 2% inflation to cut rates.

We think this pause was the right decision by the FED. We have not been surprised by the slow cutting from the FED as we have been saying rates will be higher for longer for over a year now.

Powell's statement gave little indication of what officials think comes next for interest rates, leaving the FOMC flexibility to respond to data and other economic policy news. We think this was purposeful as there is a lot of uncertainty on how looming tariffs could impact the job market and price growth.

On a side note, at Powell's press conference, he said he has no contact with Trump and will not comment on the President's remarks regarding the FED and his leadership. Ironically, Trump nominated Jerome Powell to his position in February of 2018.

The FED's next policy announcement is March 19th.

Tariffs and Canada

One last story in this week's edition, we are not sure of the validity of the statement, but it looks like there is a way for Canada to avoid tariffs from the U.S. and it does not involve Canada becoming a U.S. State. According to Trump's nomination for Commerce Secretary, Canada (and Mexico) can avoid tariffs if they swiftly close their borders to Fentanyl. Trump's pick to lead the commerce department testified on Wednesday in the Senate for his confirmation hearing. Trump's pick is Wall Street veteran and billionaire Howard Lutnick. Lutnick was the CEO of Cantor Fitzgerald a middle-market investment bank.

Lutnick said these tariffs are a threat from Trump and if the Canadian government acts quickly, there will be no tariffs. Lutnick shared similar thoughts to Trump regarding overall trade policy pointing to a universal 10% tariff on imports, and strong regulation on China's access to U.S. technology. He also mentioned that his department will focus on expanding the U.S.'s access to Canada's dairy market. Lutnick echoed Trump's thoughts on the EU ripping the U.S. off. Lutnick also claimed China stole things to develop DeepSeek. He vowed to put that practice to an end as Secretary of Commerce.

So, Canadians could potentially breathe a sigh of relief if our government closes the border and makes it more secure. We hope these claims from Lutnick are true and the Canadian government acts accordingly.

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