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.

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

Les Eclaireurs Lighthouse - Beagle Channel, Tierra del Fuego, Argentina

Cape Reinga Lighthouse - North Island, New Zealand

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

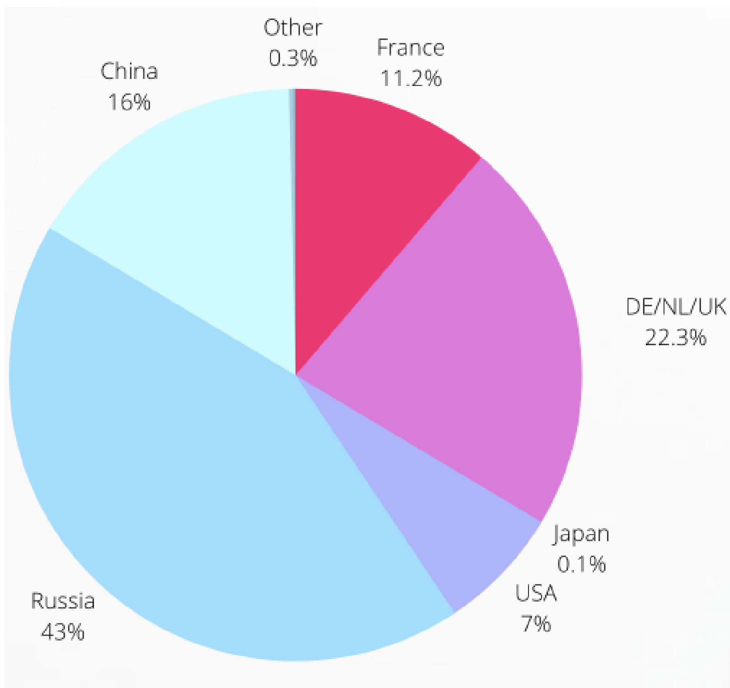
More Implications of Russia Ukraine

In the last two issues of *The Weekly Beacon* (March 4th and February 25th), we have highlighted some of the sanctions the West has placed against Russia. We have also highlighted what will happen to financial markets, specifically in commodity markets.

The biggest news this week came from the U.S. banning Russian energy (oil, gas, and coal). (Note: Uranium was left off the list).

1. Uranium

Russia is the world's largest uranium enrichment provider. Uranium enrichment is a process that is necessary to create an effective nuclear fuel out of mined uranium by increasing the percentage of uranium-235 which undergoes fission with thermal neutrons.



Specifically, in the U.S. market, 16% of nuclear energy purchases were from Russia in 2020. The U.S. has a huge reliance on Eastern nations for uranium.

Sources and shares of total U.S. purchases of uranium in 2020 were:

22% Canada	**22%** Kazakhstan	**16%** Russia	**11%** Australia
8% Uzbekistan	**5%** Namibia	**14%** U.S. and five other countries combined	

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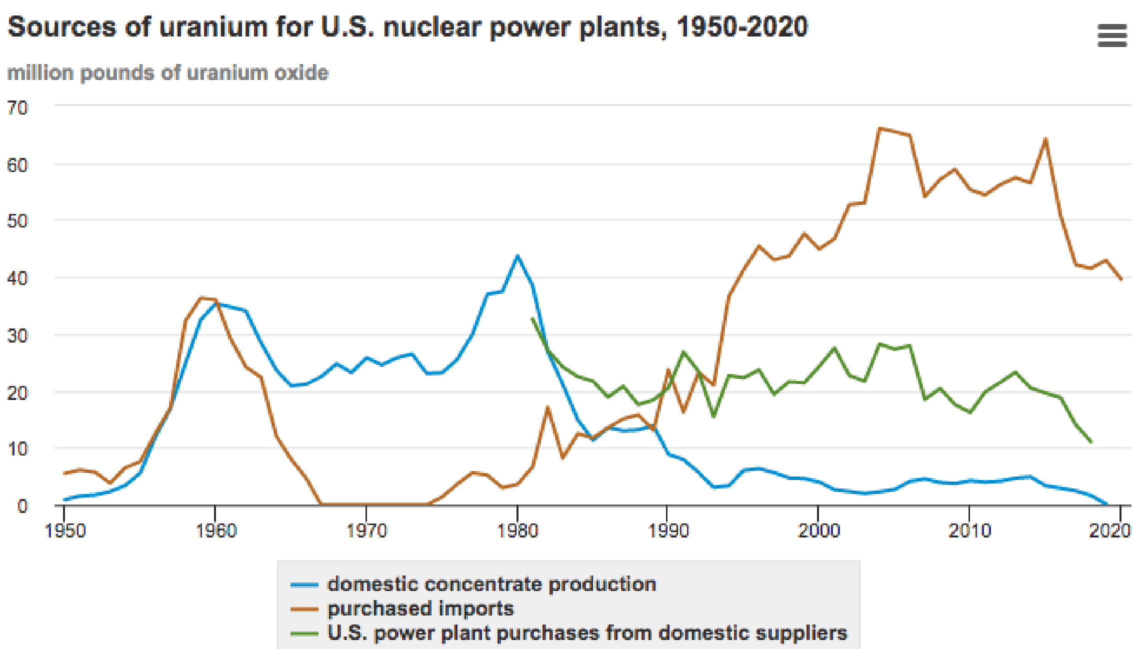
As nuclear energy will be a large part of tomorrow's economy and a source of energy that will decrease pollution, it will be critical for western nations to increase nuclear energy production (if they can). The U.S. have very small uranium reserves - Canada has the second largest in the world. France remains the only large western nation that relies heavily on nuclear energy.

The U.S. has not always relied on importing uranium for nuclear energy use. Domestic production has been on a steep decline since 1980 and purchased imports have done the reverse. If the U.S. ever wants to reach net zero, they will realize that uranium will lead the way.



Late on Wednesday afternoon the Biden Administration announced that they were considering sanctions on Rosatom, a Russian nuclear fuel producer. Rosatom is state owned and accounts for 35% of global uranium enrichment. This move would be extremely bullish for underlying uranium spot prices.

2. <u>More Countries Join the U.S.</u>

After the U.S. banned Russian energy imports, the U.K. announced Russian oil imports will come to an end by the end of 2022. Approximately 6-8% of U.K. oil imports are from Russia.

The European Union also announced they will be decreasing their reliance on Russian oil and gas.

Climate change: EU unveils plan to end reliance on Russian gas

By Matt McGrath
Environment correspondent

23 hours ago

The plan will cut Russian energy imports to 0 by 2030. The move is supposed to be in support of Ukraine but, if it takes almost 10 years, will it accomplish anything?

45% of the EU's natural gas came from Russia while 27% of its oil came from there.

The EU will attempt to cut Russian gas imports by 2/3 in 2022 by relying on domestic renewable energy sources (after this winter, has the EU not learned its lesson???? 2022 shortages here we come). The EU also announced it will accomplish these goals by saving energy and diversifying supplies (energy rationing does not sound fun). Officials released documents showing that substantial new supplies of natural gas could come from countries like the United States, Qatar, and Egypt. The problem, though, is that Europe will need to compete with other major consumers like China, South Korea, and Japan, and the additional demand from Europe might push prices up higher for everyone.

The aim is to have gas stocks at 90% of capacity by the Autumn, up from around 30% now across the EU (demand surge). In the short term, some countries may need to use more coal in the months ahead.

Europe's energy policy has failed the entire continent and is a major contributor to surging global prices. They went green before green was ready and outsourced their fossil fuels to a geopolitical foe, Russia. Even Elon Musk took a shot at Europe:

We are sure you notice our consistent nuclear commentary.

3. Ukraine and Agriculture

Ukraine does not have a massive economy and does not jump off the page in terms of technology. They are home to the 35th most people on Earth (larger than Canada), the 60th largest GDP (Ukraine's GDP is lower than Angola, Kuwait, Romania) but they are an important country in terms of products they export.

Although Ukraine was only the 46th-largest exporter globally in 2020, it does specialize in certain goods, and the world does have a reliance on Ukraine for these goods.

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Ukraine was the fourth-largest exporter of maize globally in 2020 (behind only the US, Argentina, and Brazil). Ukraine exported $4.9 billion worth of maize, accounting for 13% of the world's total maize exports. Ukraine was the 4th exporter of barley (12% of total world exports), 5th exporter of wheat and meslin, and the world's largest sunflower oil and sunflower seed exporter.

Wheat and commodity prices have soared over the last few weeks as Ukrainian farmers and companies will not be able to plant during the upcoming season. A shortage is likely this summer for many of these agricultural products. Fertilizer prices have also soared. Food will become more expensive.

Wheat is double the price it was in 2020 and triple the price it was in 2017:

Ukraine also plays a critical role in other global commodity markets. In 2020 Ukraine was the 2nd largest exporter of iron or non-alloy steel (semi-finished), 3rd largest exporter of pig iron, and 9th largest exporter of ferro-alloys.

China is Ukraine's largest export partner. In 2020, China bought $7.1 Billion of goods from Ukraine.

Prices will rise in energy markets, but also across various agricultural markets.

4. Russian Reaction to Sanctions Causing Global Nationalism and Rationing

Russia responded to the U.S., U.K., Canada, and the EU cutting Russian energy imports by slashing back at the West. In an announcement, Russia said they will be conducting a study that will eventually ban various commodities from being exported to specific countries across the world. Putin is attempting the old "You hurt me, so I will try to hurt you" move.

As a global leader in exporting various metals, agricultural goods, and energy sources, these actions by the Kremlin could have deep impacts on global market.

By threatening the world, Russia caused numerous nations to rethink their commodity exports and reliance on imports.

> Mexico considering reducing oil exports to achieve self-sufficiency in fuels and stop selling oil abroad by 2023. China has asked state refiners to consider pausing exports of gasoline and diesel. Hungary has discussed banning agriculture exports. Russia export bans are coming…
>
> 8:49 AM · Mar 9, 2022 · Twitter Web App

- **Palm oil prices soar as Indonesia curbs exports**
- **Ukraine bans wide range of agricultural exports**
- **Serbia bans exports of wheat, corn, flour and cooking oil**
- **Yara curtails fertiliser output in Italy and France**

European nations, China, Indonesia, and Mexico have made these moves to protect their security and populations. More and more moves like these in the coming weeks will probably be announced as major shortages spread across the world.

Who can fill the Russian gap in commodities?

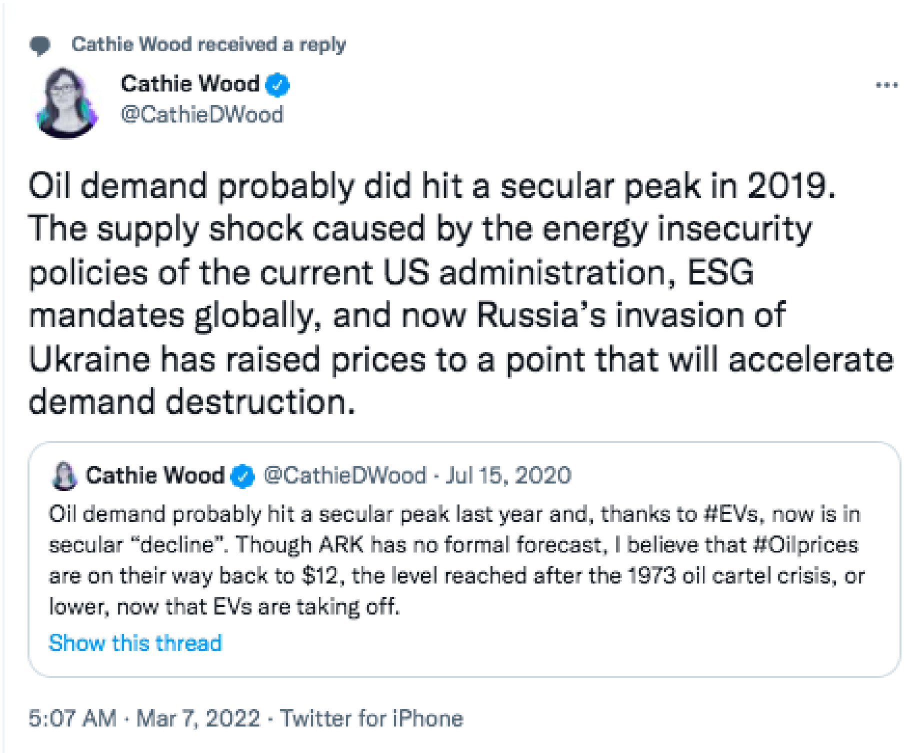
Various countries have the abilities in specific markets, but Canada could do the most in solving these supply gaps going forward. After all, Putin does not look like he will be taking a step back and it's tough to see a road where the West continues to rely on Russian commodities.

Canada has some of the largest natural resource reserves across the world. Energy, metals, lumber, we have everything. What is stopping us? Red tape from the government.

Canada's energy regulation has stunted the industry's growth over the last decade so much, that they were not mentioned in who can increase oil production to replace Russia. The Biden administration asked Saudi Arabia, the UAE, and many countries in OPEC. They even asked nuclear ambitious Iran and the Narco dictatorship of Venezuela. Why does the West not assist itself internally, Canada, the U.S., and Europe alone will not solve pollution but their leaders think they will. Energy production is a serious issue and arguably a national security issue, why depend on your enemies?

Cathie's Failure

Ark Investments CEO Cathie Wood replied to her tweet from July 2020 that predicted the price of oil. Wood predicted oil would be trading at $12/bb. At the time of this tweet, oil was trading at $40/bb.


Cathie Wood received a reply

Cathie Wood
@CathieDWood

Oil demand probably did hit a secular peak in 2019. The supply shock caused by the energy insecurity policies of the current US administration, ESG mandates globally, and now Russia's invasion of Ukraine has raised prices to a point that will accelerate demand destruction.

Cathie Wood @CathieDWood · Jul 15, 2020
Oil demand probably hit a secular peak last year and, thanks to #EVs, now is in secular "decline". Though ARK has no formal forecast, I believe that #Oilprices are on their way back to $12, the level reached after the 1973 oil cartel crisis, or lower, now that EVs are taking off.
Show this thread

5:07 AM · Mar 7, 2022 · Twitter for iPhone

Even though oil has more than tripled in price since that tweet and has a 52-week high of $130/bb which is the highest price in 14 years, Wood doubled down on her horrible prediction. According to Ark, oil demand is on the decline due to electric vehicles, ESG guidelines, and Russia invading Ukraine. We think the "demand destruction price" is much higher than Wood and other analysts are claiming. Average consumers who bought a car over the last few years are not suddenly going to buy an EV on a whim.

We are not sure where Wood gets these narratives from but, a simple Google search would prove oil consumption and demand are growing. Global oil consumption will be higher in 2022 than it was pre-pandemic and oil consumption is expected to grow for years to come. Billions of people live in poverty across the world, the best way to get people out of poverty is providing energy. Providing impoverished African and Asian nations with solar panels and wind turbines seems quite expensive. Oil and gas demand will continue to grow. Prices will decline but, not to $40/barrel let alone $12/barrel.

The one thing nobody can deny, Ark is bullish on EVs. The weirdest part of Ark, out of all the funds they have launched, they have not bought any mining or exploration companies. No matter what brand of EV you talk about, they all require the same metals to be produced. If Wood is so bullish on the sector why does she not buy a basket of Cobalt, Nickel, Copper, Lithium, and other rare earth metals. Even if her fund is not allowed to invest in this, she could easily create one that would. She created a private

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markets fund over the last few months and a space exploration ETF in 2021. She has the capabilities to add to her portfolio of funds.

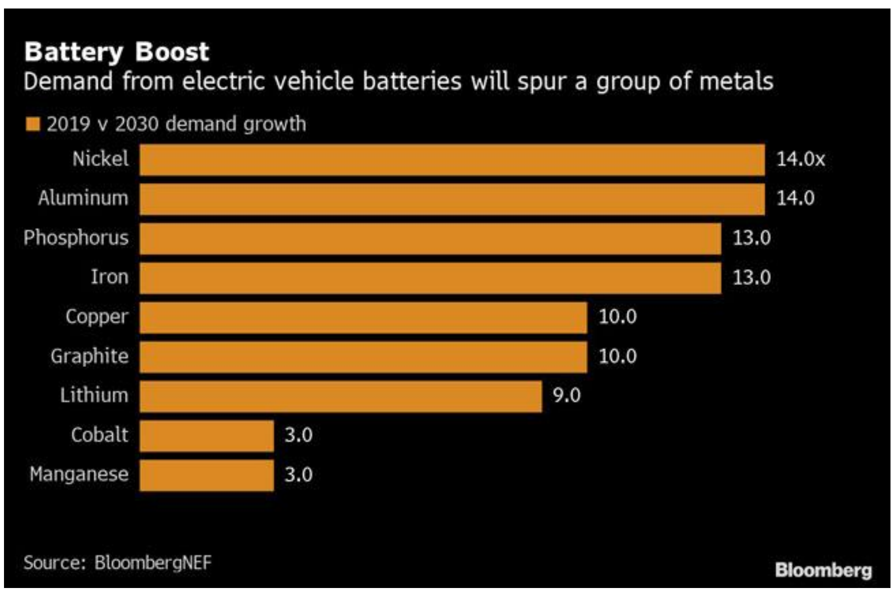

Lawrence McDonald @Convertbond · 19m
The innovation sales pitch is great - but why isn't ARK long the necessary metals - commodities needed to fulfill the pollyannish view? Airball?

#Cobalt
#Copper
#Nickel
#Uranium

Seems very weird for the Queen of EVs.

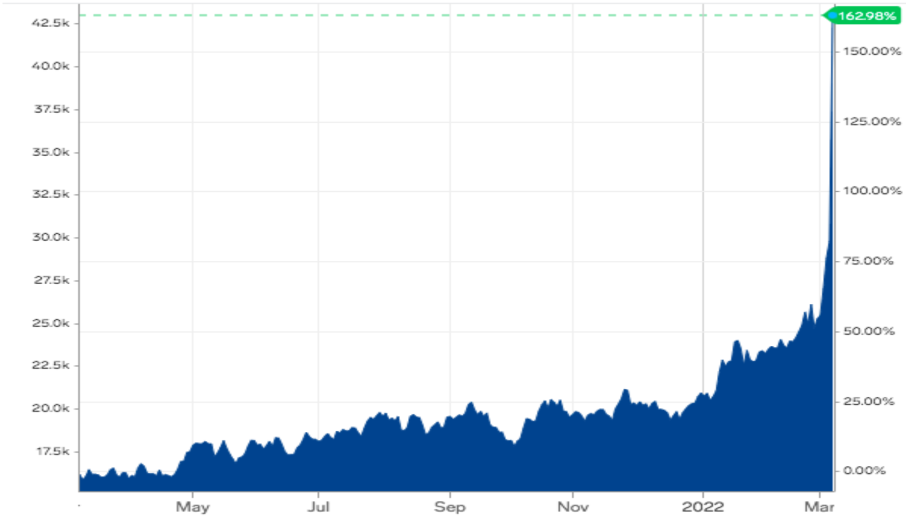
Speaking of EVs

As we are sure you are aware, Nickel is a major input in EVs. Demand growth will balloon as demand increases for EVs.

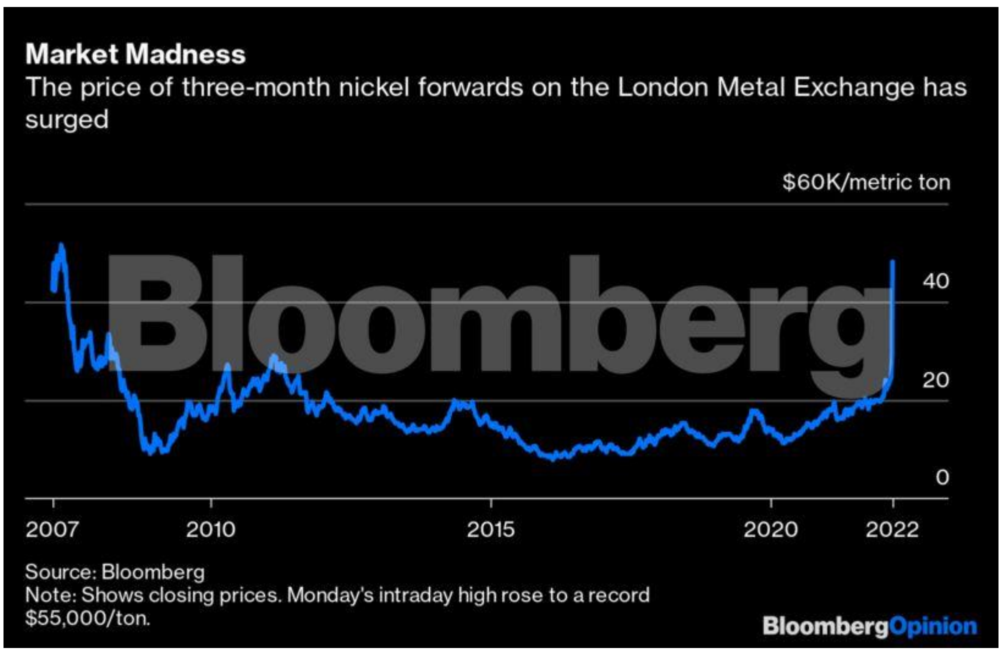


Well, EVs could get a whole lot more expensive and it's because of Nickel prices.

Nickel prices have surged over the last year but, increased at an exponential rate over the last week. Prices surged so quickly that the London Metals Exchange stopped Nickel trades for parts of Tuesday.



Zooming out the price move is a lot more violent.



The highest price since 2007.

Why did prices surge so quickly this week? Russia.

Russia is the world's 3rd largest producer of Nickel. Nornickel, a Russian miner is the world's largest private producer and miner of Nickel. Russia accounts for approximately 33% of the world's Nickel sulfide ore (high-quality pure Nickel). Russia is the world's largest producer of Class 1 Nickel (high-quality pure Nickel). The world reacted in a negative way to supply worries. We think the move is an overreaction in the near term but, some foreshadowing for the future in terms of rare Earth metals pricing.

This price move has increased the cost of producing an EV by $1,000, according to Morgan Stanley. EVs will continue to get more expensive as the demand for these rare Earth metals grows.


yahoo!finance | Yahoo Finance

Nickel price surge could add $1,000 to production of an electric vehicle: Morgan Stanley

Pras Subramanian · Producer/Reporter
Tue, March 8, 2022, 12:57 p.m. · 3 min read

Zooming out on the Markets

This week we wanted to bring you some macro charts on financial and equity markets.

Chart #1: Energy Alone

Energy is in a world of its own in 2022. It is the only sector on the S&P 500 that has produced a positive return through the first 60 days of 2022. The sectors hit the hardest have been technology-related and it's no surprise why - valuations. If you had little to no exposure to oil and gas, you have had a cold start to 2022.

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Chart #2: Record Levels

The U.S. Market Capitalization of all stocks remains extremely above the U.S. GDP. This chart has famously been coined the Buffett Indicator. Warren Buffett has looked to this chart throughout history when pointing to extreme valuations and inconsistencies between the economy and financial markets. With the recent drawdown, the U.S. Market Cap to GDP ratio has declined from over 200% to 175%. At this level, we are still at historical highs, to reach the peak of the Dot Com Bubble we would need a further drop of 15%. Stocks are still not cheap, and the economy is nowhere near as healthy as the media say.

Chart #3: Historically Bad

US equities performance in the first 44 trading days (123 years history)

	THRU DAY 44	DAY 45-DAY 250
1/1/2009	-24.3%	49.0%
1/1/2022	-11.9%	
1/1/1920	-11.8%	-24.8%
1/1/1935	-11.1%	52.4%
1/1/1982	-10.8%	25.6%
1/1/1900	-9.9%	6.0%
1/1/2008	-9.2%	-31.4%
1/1/1968	-9.1%	8.2%
1/1/1960	-8.9%	5.4%
1/1/1978	-8.6%	10.3%
1/1/1948	-7.8%	7.6%

U.S. equity markets have started 2022 horribly. The start to 2022 has been the second-worst start to a calendar year over the last 123 years. This mild correction that has been slowly drawn out is not similar to the Financial Crisis, Dot Com Bubble, or even the Covid-19 flash crash in terms of size. However, the correction could continue as inflation, global conflict, and numerous other risk factors are still prevalent across the world.

Historically speaking, out of the worst 4 performances to start a year (previous to 2022), 3 have created positive returns over the remainder of the year, the one exception was way back in 1920.

Chart #4 and #5: Early Innings of a Commodity Boom?

Both of these charts show how undervalued or relatively cheap commodities are relative to the S&P 500 (stock prices). Stock prices have surged over the last 40 years but especially over the last 10 years. Anyone who says we are currently in a commodity bubble should be shown this chart, the bubble has not even begun.

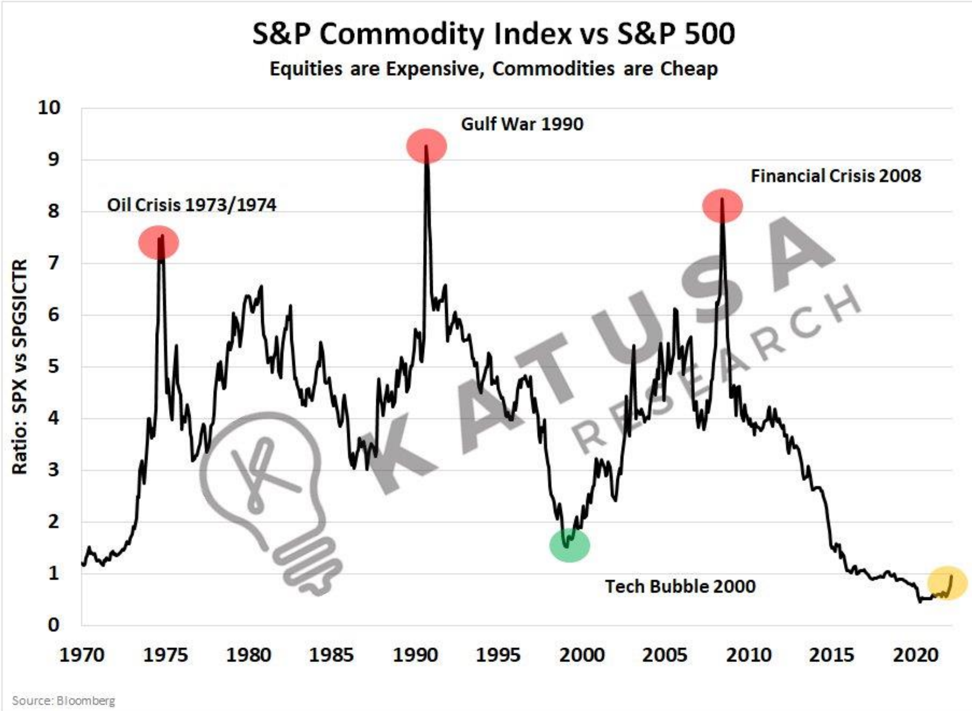

Chart #6: Energy vs. Technology

The last 20 years have been *quite* kind to technology stocks. The last 10 years have been *very* kind to technology stocks, and the last 5 years have been *extremely* kind to technology stocks. We are not being redundant and labeling every technology stock as overvalued, there are a few that have tremendous value and positive cash flows (they will stick around). Our point is, hundreds of technology companies have been propped up by the market leaders and have been dragged along to wonderful returns based on comparison and disruption (not earnings and valuations).

We think going forward certain energy names will greatly outperform the market unless policy changes soon. The supply-demand gap going forward in energy is a real crisis. Some energy companies have the best balance sheets they have ever had and are paying their profits back to shareholders.

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March 11, 2022