

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.*



Robbins Reef Light, Upper New York Bay



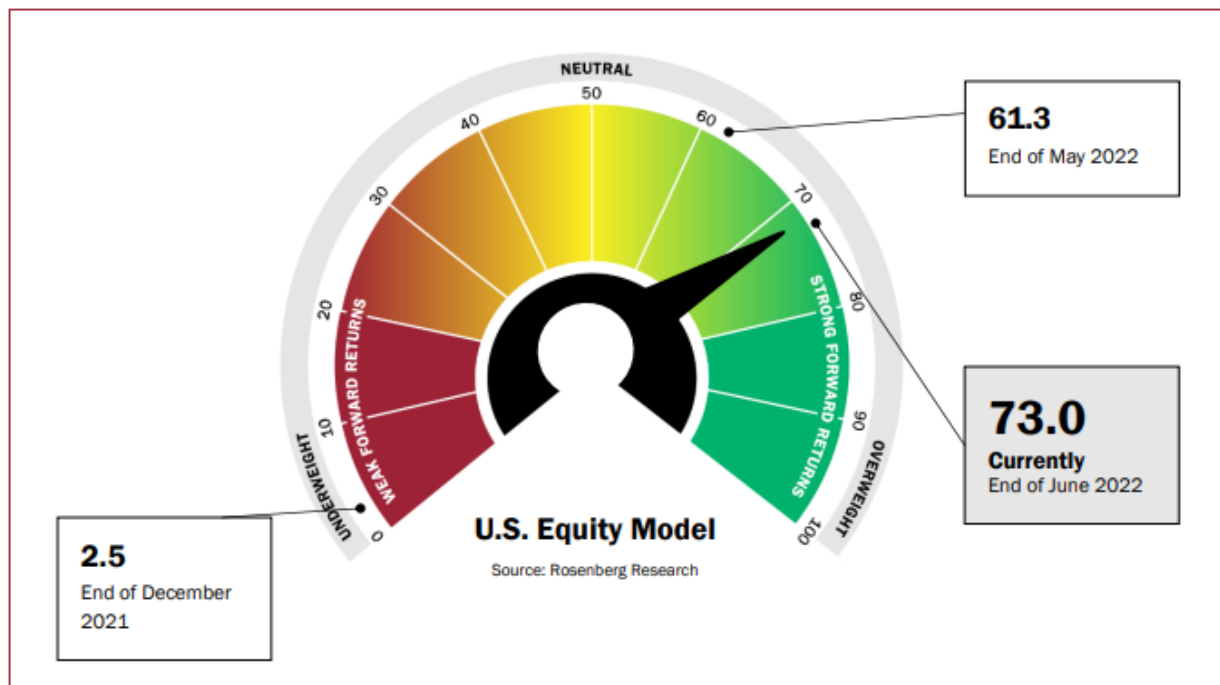
Les Eclaireurs lighthouse, Argentina

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

A Different Outlook

We have often mentioned some of our partners, whether that be our economic consultants, external fund managers, or analysts in this publication. We believe they bring a point of view that can help our readers. This week we wanted to highlight David Rosenberg's Market Strategizer which he publishes via Rosenberg Research, a platform that shares economic information with investors. [Click here to visit Rosenberg Research and to learn more about them.](#)

One of Rosenberg's most important indicators is its U.S. Equity Model which calculates how attractive U.S. equities are as a whole over time. The higher the number, the more attractive and vice versa.



At the end of June, U.S. equities seemed quite attractive from an economic standpoint. At the peak of the markets in December 2021, Rosenberg predicted a massive sell-off due to his indicator being at 2.5 out of 100. Boy was he right. So, during the selloff, we have come a long way, but that does not mean a bull market is ahead for Rosenberg. He still sees a downside in the markets, at least in the short term. The U.S. Equity Model is nowhere near its all-time high. In April 2020 it read 100% and Rosenberg said it was the strongest buying opportunity since 2009. So possibly there will be some more downside but that's not a surprise. Rates are on their way up, inflation remains elevated, and major recession fears are plaguing Western nations. We will continue to share this Equity Model with our readers at major inflection points.

On a sector basis, Energy remains the strongest sector on Rosenberg's U.S. and Canadian Major Sector rankings. Even with the sell-off, his calculations which use fundamentals, technicals, valuations, and positioning still have energy equities as the strongest sector. We hope the recent sell-off has not scared any of our readers. Oil and natural gas equities could be poised for a run after being oversold over the last 3-4 weeks. Rosenberg highlights the Free Cash Flows being produced by these energy companies which we have mentioned numerous times over the last year. Rosenberg also states "We could get a

significant decline in the underlying commodity price and the profitability and ability to return cash to investors would not be impaired” when describing the bull case for energy stocks. Companies are buying back stock, paying off debt, and paying dividends at rates we have never seen. These companies will be cash cows going forward.



Rosenberg is not one of our major partners that we use for energy research as he is an economist by trade, but when even his indicators are pointing to energy, we know the sector could see some fireworks going forward.

Inflation Galore

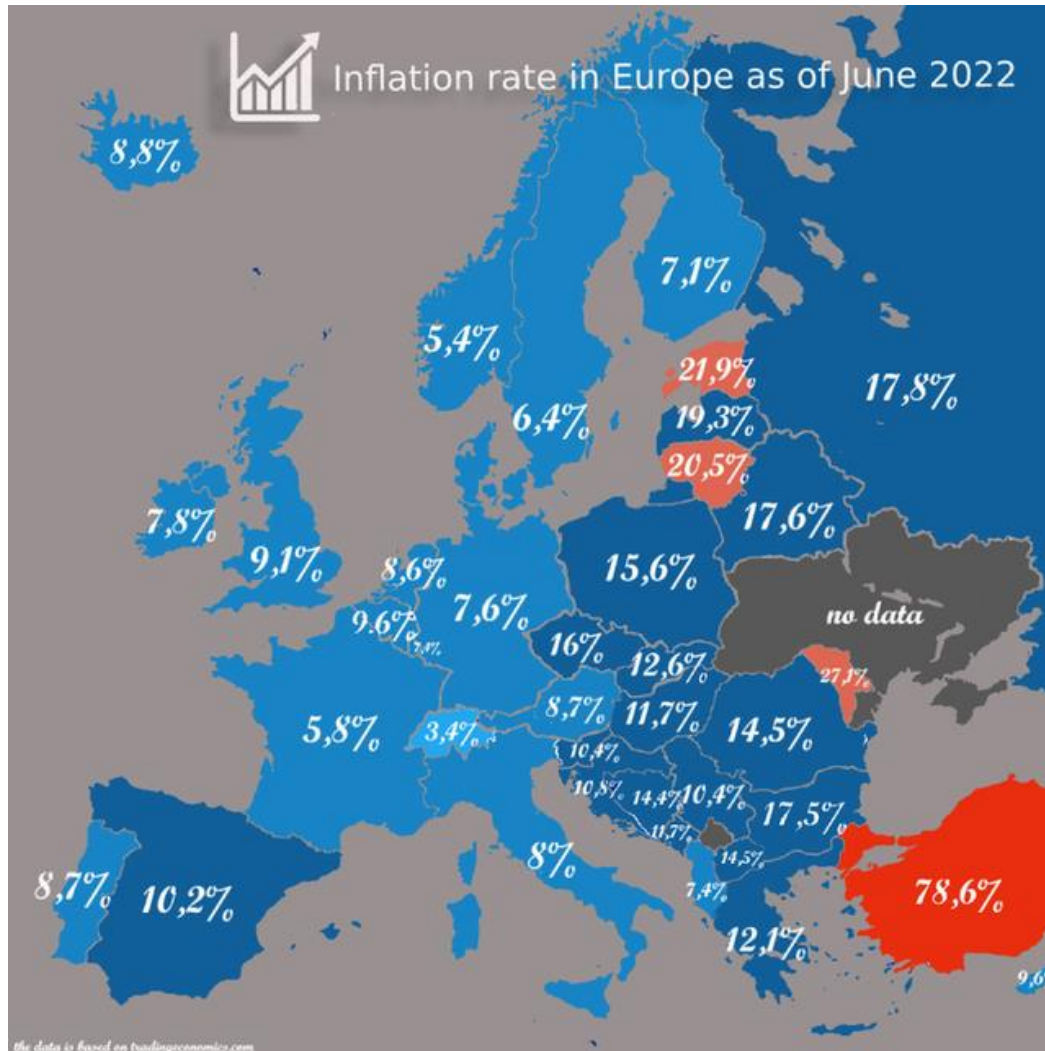
On Wednesday the U.S. Bureau of Labour Statistics released the June 2022 Consumer Price Index and boy was it high.... another month, another record. Team transitory must be ill by this point.....

US June CPI +9.1% y/y vs +8.6% expected

• US June 2022 consumer price index inflation data

June's number was yet another 40-year high for the CPI (feels like we say that every month). After months of record-level inflation and a shrinking economy, President Biden being compared to President Carter seems fair. Even looking beyond the economy, the Biden Administration cannot get a win. The likelihood of him being a one-term President is becoming more likely. The economy and stock market have become larger issues in recent years and voters will not forget what happened in 2021 and 2022.

If the reported (we think inflation is much higher than 9.1%) U.S. numbers are not enough for you, look at this chart on inflation in Europe by country.

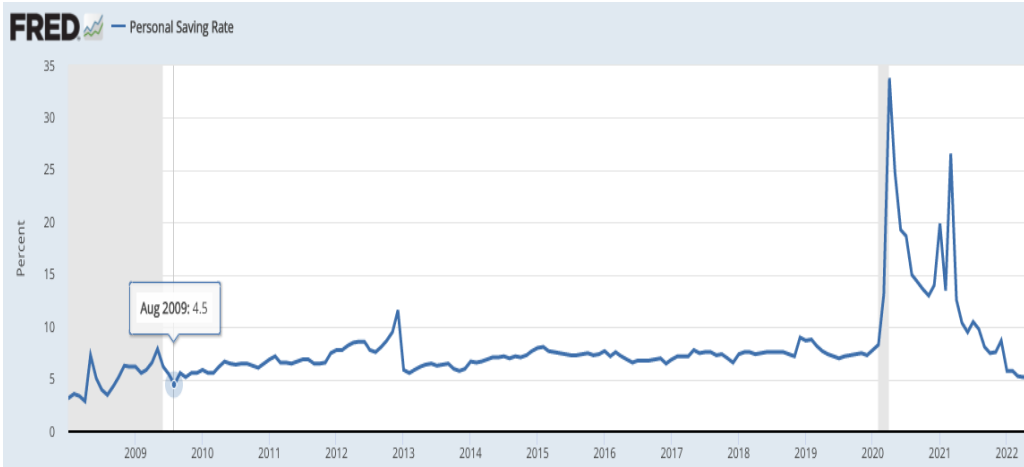


This is not a map of third-world countries with terrible economies. This is a map of completely industrialized Europe. Eastern and Central Europe all are reporting inflation above 12%, most much higher.

If that's not bad enough, that 78.6% is for Turkey, a G20 and NATO nation. Turkey is home to the world's 19th largest economy in terms of Gross Domestic Product and is a major bridge (negotiations) between the East and West.

After 78.6% inflation and the Lira collapsing, the Turkish Bank has placed a 19.9% target on inflation by the end of 2023. The Lira might have been the biggest Ponzi of them all after this.

Regardless of where you live, inflation is killing wallets. It's no surprise the U.S. savings rate is at its lowest point since August 2009 (the last major, sustained financial crisis).



The most recent release by the U.S. BLS for this was 5.4% for May. We would expect this to drop in the coming months. Consumers are dipping into their savings to afford all kinds of price increases. We would expect the savings rates to mirror the trend we have seen in the U.S. across the rest of the industrialized world.

A user on Twitter has been cleverly updating a pay raise chart compared to inflation since the fall of 2021.



The real question going forward: will we hit double digits in the U.S. (for what is reported)? We do not think so due to energy prices rapidly dropping in June and other prices starting to ease due to less demand. The fears of a coming recession are also growing which could also bring down inflation.

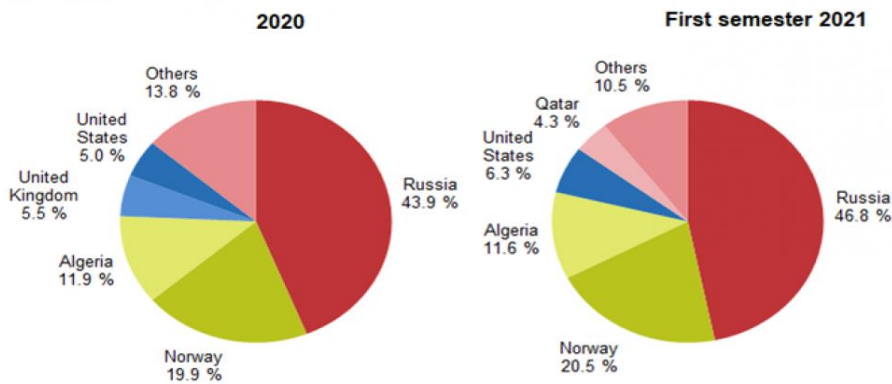
Germany, an ongoing failure

When historians look back on history and look at the great rotation from fossil fuels to renewable and clean sources of energy, it will be a short chapter. They will skip to the point where clean energy overtakes fossil fuels like oil and coal. What they might miss is the decades of failures due to horrible policies initiated by Western countries, the biggest failure being Germany. We have nothing against Germany, and they remain an economic juggernaut within the EU, but what is happening there is appalling and is 15-20 years in the making.

We have often ridiculed their energy policy. They hate fossil fuels, hate nuclear, and love solar, wind, and hydro. Beginning in 2000, Germany has spent hundreds of billions of Euros on transition energy sources. By 2019, 41.1% of German electricity came from renewables (renewables had the potential capacity to source 54% of the country's grid). That was all well and good until 2011 when Chancellor Angela Merkel announced the country was turning away from nuclear energy. This pushed more renewables and basically was close to eliminating nuclear energy use in Germany in a matter of 10 years.

Fast forward to this year after Russia invaded Ukraine and Germany is in a major pinch. Their power grid which had already been struggling in 2021 due to supply shortages stemming from renewable reliance was placed under further pressure due to Western sanctions placed on Russia. Even though Germany focused on renewables, they still used fossil fuels and almost all of those fossil fuels came from Russia. Germany's energy grid was in the hands of a geopolitical enemy. This was a national security risk for all of Germany. Around 95% of natural gas in Germany is imported and a majority of that has historically been from Russia.

Extra EU imports of natural gas from main trading partners, 2020 and first semester 2021
(share (%) of trade in value)



Source: Eurostat database (Comext) and Eurostat estimates

eurostat 

The interesting factoid of Germany's energy policy is that they have barely cut back on their Russian energy imports. They are being held hostage and the west is not giving them any real solutions. Germany's solution seems to be more investment into green energy. Yet another German failure.


Germany plans \$216bn green energy investment to ease Russian gas reliance

► Electric charging infrastructure and hydrogen fuel to receive financial boost amid Ukraine crisis

Renewables could be the answer, but they are not the short to medium-term answer.

A thread was going around Energy Twitter this past week and there are two tweets we wanted to share with you, both courtesy of an American journalist, one from 2017 and one from this month.

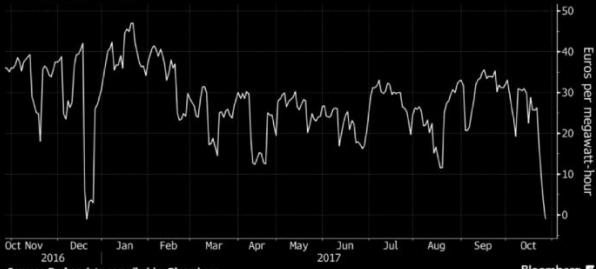


 **Joe Weisenthal**
@TheStalwart

Germany is producing so much renewable **energy**, homeowners might get paid to use electricity this weekend [bloomberg.com/news/articles/...](https://www.bloomberg.com/news/articles/)

Price Holiday
Weekend price negative first time since Christmas

■ German weekend Power Price



Oct Nov Dec 2016 Jan Feb Mar Apr May Jun Jul Aug Sep Oct 2017

Source: Broker data compiled by Bloomberg

Bloomberg

12:42 PM · 10/26/17 · TweetDeck

 **Joe Weisenthal**
@TheStalwart

"**Germany** says gas shortfalls could trigger a Lehman Brothers-like collapse, as Europe's economic powerhouse faces the unprecedented prospect of businesses and consumers running out of power."

[bloomberg.com/news/articles/...](https://www.bloomberg.com/news/articles/)

So much for all that surplus renewable energy. Renewable energy seems like something that is not there when you are desperate but when it is there you may not need it.

Deutsche Bank put out a global energy analysis and what they say about Germany is quite dystopian for a G7 nation.

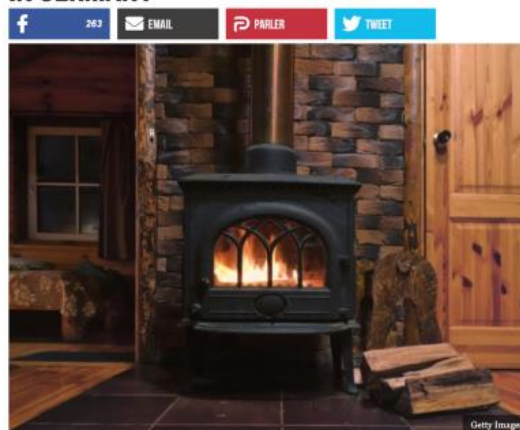
comparison even though it is below the recent peak of roughly 3,000 GWh per day. The Netherlands and Norway have already increased their exports to Germany since late May by roughly 20% (with significant volatility).

- Regarding German gas consumption, **we expect that demand will remain some 10% below the respective level one year ago** over the next few months. This reduction is driven by savings of private households, industry, and the services sectors, incentivised by very high gas prices. The overall weaker economic development will dampen gas demand in the manufacturing industry. In addition, **substitution of gas by other energy sources (hard coal and lignite in the power sector, wood for heating purposes in private households where possible,** switch to oil derivatives in the industry, etc.) contributes to lower gas demand. Both savings and substitution have already led to a reduction in German gas consumption by more than 14% yoy in the first five months of 2022. However, large shares of these savings are driven by the mild winter 2021/22 which is why we assume a reduction by another 10% "only".

The investment bank is modeling German households switching from gas heat to wood burning (out of necessity due to fuel shortages in the cold winter). We are not discounting the benefit of a wood-burning fireplace but as a primary source of heat during a Northern Hemisphere Winter, perhaps this issue is even worse than we have forecasted.

Even wood will not solve this issue. Germans are flooding stores to stock up on wood for the coming winter. The only issue, there is a shortage of wood in Germany.

IMPORTED ENERGY CRISIS SEES WOOD BURNING STOVES, DRY FIREWOOD SELL OUT IN GERMANY



Germany is the hotspot of a bad policy on energy - underinvestment, overregulation, no solutions, no expansions, and a war in Europe. We hope people finally wake up (they probably will not). Perhaps it will take a long, cold winter to wake them up.

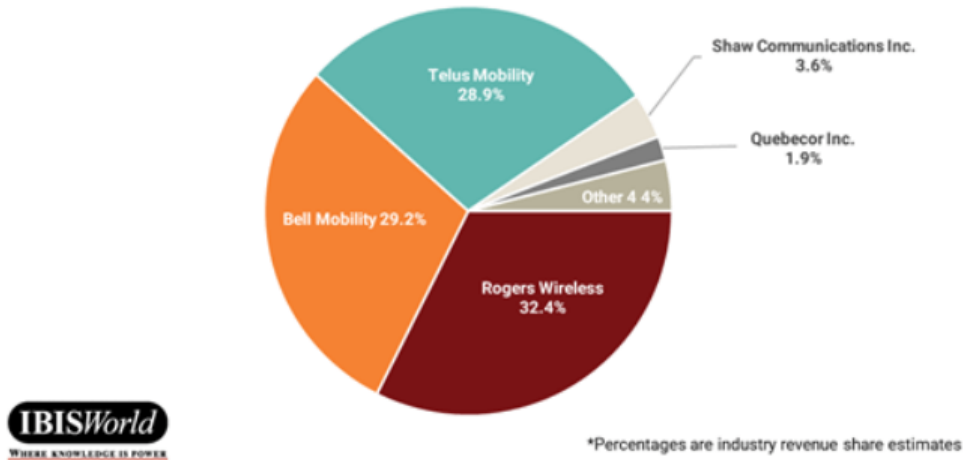


Finally, Time for Change?

The Canadian Phone, Television, and Internet services sector are an oligopoly.

The Telecom Market is served by 3 companies. The issue is the 3 companies do not compete, they congregate. Bell and Telus often share cell towers across the country, and Bell and Rogers co-own the most popular sports team in the country together (Toronto Maple Leafs). No matter how you slice it on the ownership side, there is no way Uber and Lyft would co-own the San Francisco 49ers or Nike and Adidas would co-own any other sporting team.

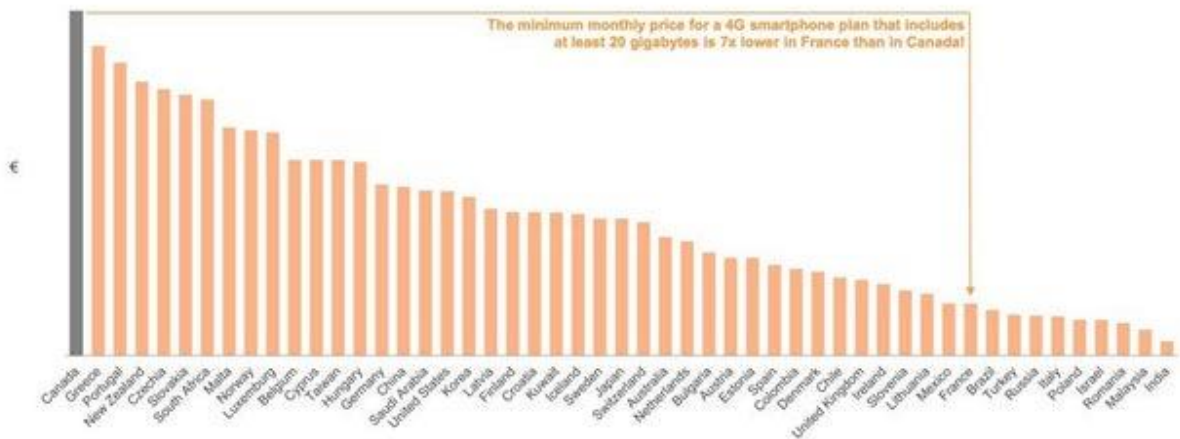
Breakdown: Canada's Wireless Telecom Market (2019)



It's a 3-way marketplace that is home to the world's most expensive phone plans (in the first world).

Rewheel research PRO study, April 2021

MIN monthly price for 20 gigabytes - March 2021
4G&5G smartphone plans with at least 1000mins and 100Mbit/s



Minimum monthly retail price (incl. VAT & tax) for a given gigabyte allowance among all eligible tariffs logged in the database for country.



We have the highest prices in the world and remember what they did back in 2013 when Verizon, a U.S. provider attempted to enter Canada via acquisition and investment into infrastructure. They were essentially bullied by the “Big 3” out of the country. The “Big 3” hate competition because it does not serve them best. If Verizon was to enter Canada, it would have posed a significant challenge to Canada’s domestic wireless carriers, which historically have faced limited foreign competition due to federal ownership rules.

We bring this up because of what happened last Friday across Canada, which also bled into the weekend. Rogers went out. Rogers and all of its subsidiaries went dark. Basically every consumer using their cell, landline, Internet, and TV services were shut out. For an entire day, all services were down. 911 could not be reached, commerce was halted, and people could not text. The entire situation was a mess that caused serious issues that took a few days to correct.

Almost 15-hour network outage traced to maintenance update: Rogers

The issues were traced to an update that caused problems for millions. Not only were Internet, Cell, and T.V. services down, nobody could use Interac across the nation (Debit Payments). Seems like a company that big should have a backup plan. Aside from those businesses who use Rogers, businesses could not accept payment except in cash. We are still not sure how a multi-billion-dollar company in Canada with decades of history can have a problem this big that could last this long. This is not a tiny Internet Startup halfway across the world.

We only bring this up for a few reasons.

1. We hope this is the event that makes Tele-Comm an election issue in Canada and hope that consumers finally make a change for the better.
2. Rogers has a pending acquisition that could be stopped.

Competition in an industry brings better prices, and better services for consumers. We should all be begging for it. The oligopoly that is Canadian Tele-Comm is only good for Telus, Bell, and Rogers.

The interesting wrinkle that comes out of this outage has to do with Rogers who was set to acquire Shaw Communications, a Western Canadian telecommunications provider for \$26 billion. The transaction was approved by the CRTC in March 2022. However, in May 2022 the Competition Bureau applied to block the transaction. As the transaction is pending, the recent outage makes many of us think that the bad problem could have been even worse if Rogers was in charge of Shaw Tele-Comm infrastructure. Western Canada was not hit as hard during the outage due to Shaw having a piece of the market.

“The incident is likely to introduce incremental regulatory risk to the Shaw transaction,” BMO analyst Tim Casey said, adding that it would also raise investor concerns over Rogers’ ability to execute on deal synergies.

We highlight this as it is one of the biggest companies operating in Canada. The stock has essentially run flat over the last 5 years but has offered an attractive yield over that time period.



Market Summary > Rogers Communications Inc. Class B

59.93 CAD

-2.49 (-3.99%) ↓ past 5 years

Jul 13, 11:35 a.m. EDT • Disclaimer

+ Follow

1D | 5D | 1M | 6M | YTD | 1Y | 5Y | Max

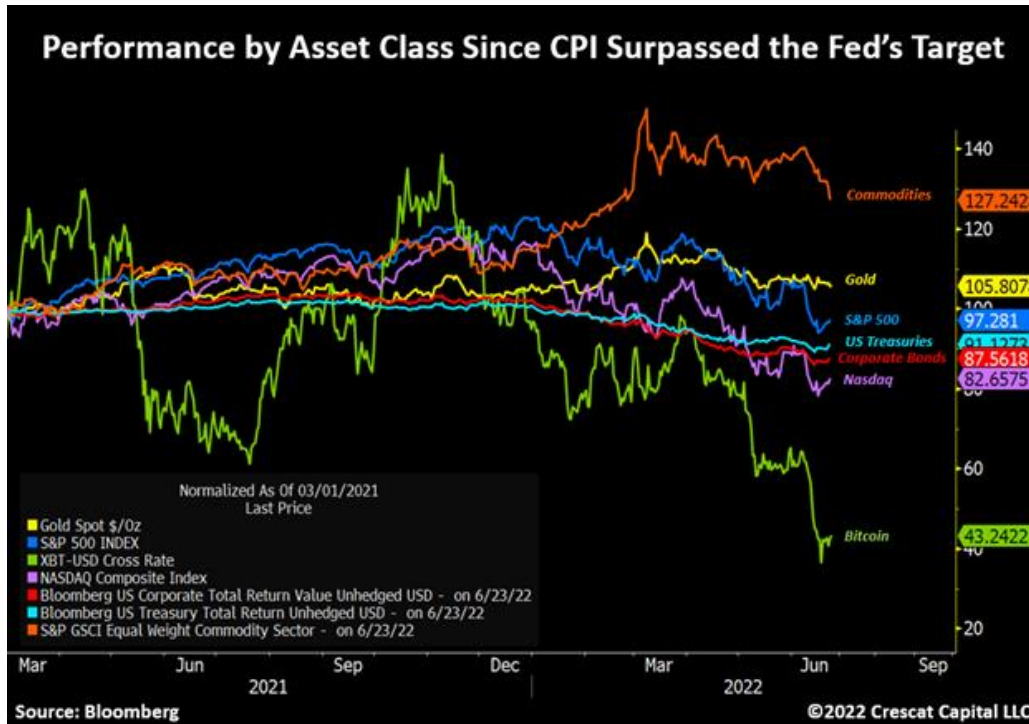


Rogers shares have traded down about 3.5% since the network outages.

Perhaps what makes Rogers stock even riskier is the premium that it is trading at. Its P/E ratio is over double the value of Verizon and AT&T's P/E ratios. Rogers also has a P/B ratio of 2.80 while the average U.S. Tele-Comm stock trades at 1.92x. While we think Canada has more value in terms of equity markets than the U.S., this subsector might be the exception. Both Verizon and AT&T also offer better yields than Rogers.

Asset Class Performance

Below is the performance of every major asset class since inflation ticked above 2% which was way back in March 2021.



Many Bitcoin Holders will cite Gold's underperformance as a major indicator of Gold failing as an inflation hedge. They will point to gold miners' underperformance as a further price drop in the spot gold price. Even though gold prices have dropped below \$1800 and are down significantly since May, the price of gold is holding on (up 5%). This is happening while Bitcoin (its supposed competitor) is down 57% since March of 2021. We hope you were not convinced to buy at the peak by somebody. We are sure this family Thanksgiving will have different conversations surrounding Bitcoin than last!

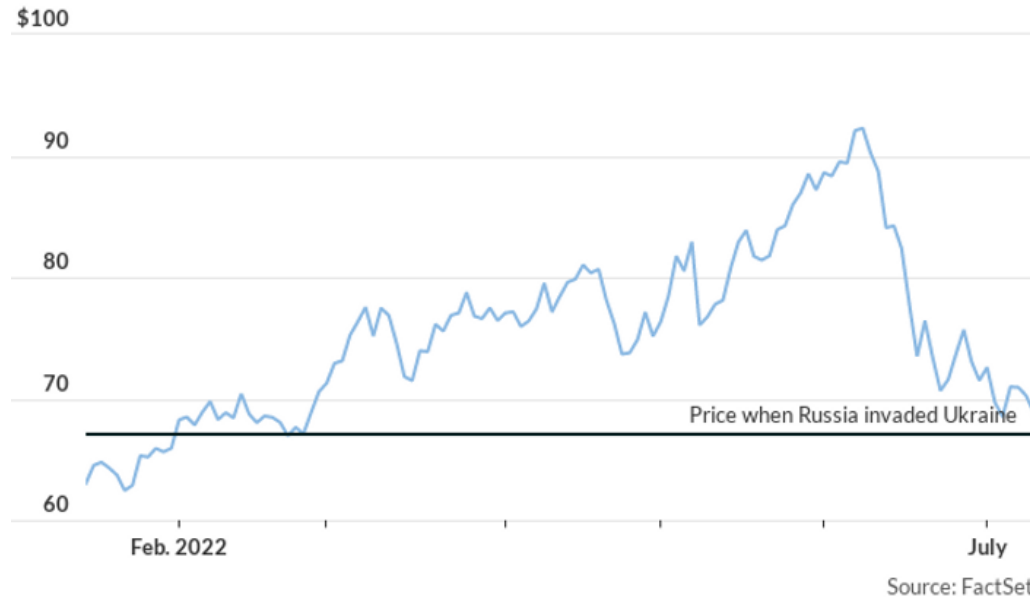
Even with the recent pullback in commodities, they have by far been the best investment since March 2021. We think commodities including gold will come roaring back and in a big way. Shortages are not solved, and sell-offs were overstated. Let the traders sell and let investors buy. We do not recommend any of our reader's "trade".

Did Demand Change?



Investors have fled the energy sector

Energy Select Sector SPDR ETF



The SPDR Energy ETF is basically at the same price it was when Russia invaded Ukraine. The market is pricing in a steep recession or a resolution in Ukraine. A resolution is not on the horizon and demand will not change especially in the short term unless something massive happens. For the supply side, no cap-ex expansion, continued regulation, no OPEC+ spare capacity, and under-producing quotas. There are no solutions for these problems being proposed that will help.

MacNicol & Associates Asset Management Inc.

July 15, 2022