

## 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.*



St Joseph Island Light House on Lake Huron from Barry B.



Nine Mile Lighthouse, Simcoe Island, Ontario

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



## Mortgage Rates Set More Records

The U.S. 30-year mortgage rate spiked to 6.29% last week setting another multi-year record for the mortgage market. This is the highest level for the 30-year since October 2008. Comparing today's rate to 18 months ago is staggering, it has more than doubled and could triple if interest rates were to continue to rise.



This has caused housing markets across the world to slow down after being red hot for almost 2 years. Even though the housing market has slowed, supply is still a major problem that is keeping prices elevated close to all-time highs.

The lack of affordability is driving a significant slowdown in the housing market. The median American household would now need to spend 44.5% of their income to afford payments on a median-priced home in the US, the highest percentage on record with data going back to 2006.

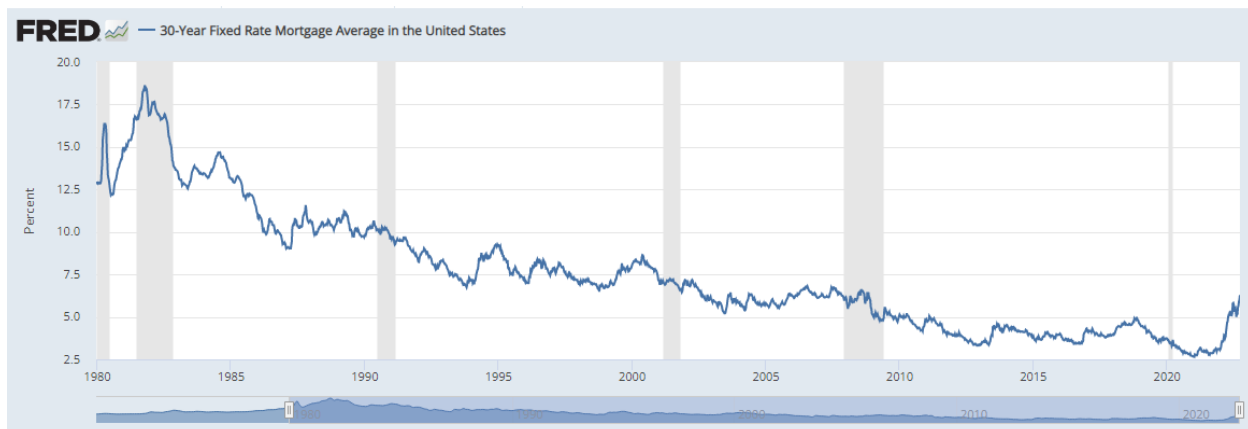
As Americans spend more and more on their mortgage payments, it is getting more expensive to live in various Metropolitan areas. Comparing 2022 salaries to affording the same homes in 2020 some of the largest jumps in income needed (to afford a home) are across southern U.S. states (Texas, North Carolina, Nevada, Oklahoma) where the population has grown the most during the last 2.5 years. This is a major reason why; southern housing prices have not dipped as much as markets in northern states and California.



Income Needed to Afford a House			
to Afford Typical Home at 30% of HH Income			
Rank	Metro, State	2022 Income Needed	2020 Income Needed
1	Austin, TX →	\$160,126	\$76,166
2	Boston, MA	\$170,841	\$99,434
3	Charlotte, NC	\$95,438	\$45,995
4	Columbus, OH	\$81,974	\$46,593
5	Dallas, TX	\$110,406	\$56,837
6	Houston, TX	\$87,909	\$48,994
7	Indianapolis, IN	\$67,815	\$36,272
8	Las Vegas, NV	\$106,652	\$51,553
9	Los Angeles, CA	\$222,184	\$123,329
10	Miami, FL	\$117,627	\$57,446
11	Oklahoma City, OK	\$55,676	\$31,523
12	Philadelphia, PA	\$93,269	\$55,004
13	Pittsburgh, PA	\$57,093	\$34,746
14	Seattle, WA	\$192,812	\$102,129
15	Washington, DC	\$139,453	\$84,828

\*Income Calculated based on Mto Payments & Prop Taxes at 30% DTI (Sources: Zillow / Census)

Jumping back to the 30-year mortgage rate which is at a decade high but nowhere near its all-time high..... Easy money has led society to believe everything is simple. Imagine the 30-year mortgage rate above 10% like it was from 1980 to 1991.



We do not think the FED will allow this to happen and would dramatically cut rates, but it is something to keep in the back of your mind when people say it is the worst housing market ever.

We encourage our readers to learn more about our MAC 360 Degree Real Estate Fund and how we approach Real Estate investments. [Click here to learn more about the fund](#) or email [info@macnicolasset.com](mailto:info@macnicolasset.com) with any Real Estate related questions.



## World Bank Slashes Economic Growth Numbers

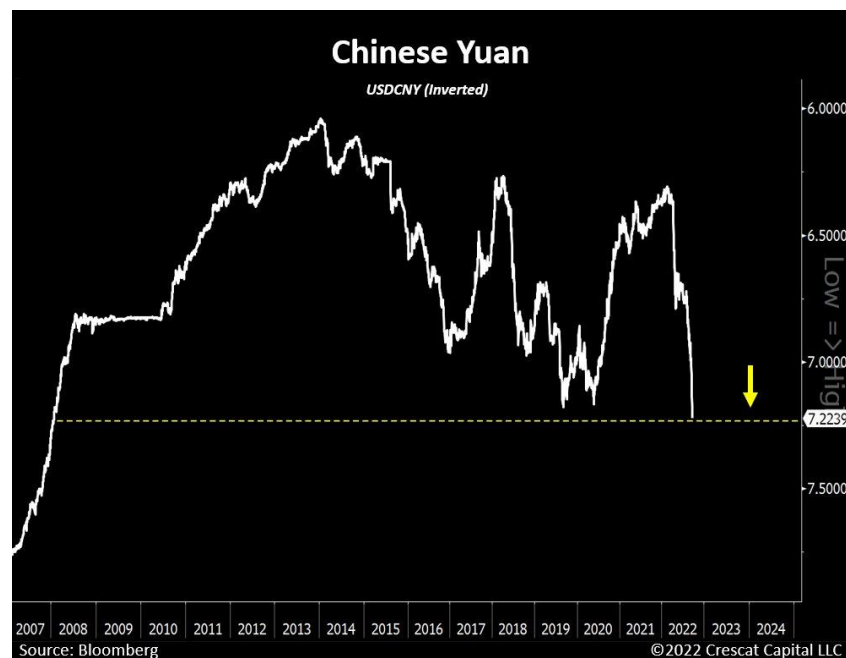
On Tuesday, the World Bank downgraded its 2022 China growth outlook to 2.8%. In a bad year, 2.8% economic growth is good, but it is a steep decline from the projected 5% GDP growth projection set out in April. A slowdown in economic activity cuts into company profits decreases capital investment and increases unemployment. This means China's growth will be weaker than the rest of the Asian-Pacific region for the first time in three decades.

China's zero-Covid policy was the main specter haunting the economy, analysts said. "Last quarter, firms told us they would not invest, borrow, or hire until their Covid-zero nightmare was over. The nightmare continues," China Beige Book said.

Eventually, China will need to move on from Covid zero like the rest of the world has returned to pre-pandemic life. China has even continued Covid stimulus through recent lockdowns as a way of propping the economy up. This has helped retail sales bounce back but has not helped the manufacturing sector whatsoever. Many insiders proclaim that President Xi and his inner circle care more about health than the economy getting back on track.

While this is an area of the world that our investors have extremely limited exposure to, we continue to caution our readers on investing in China. China's property market is in shambles. Western investors are finally waking up to the risks that China poses, and a slowing economy makes investing in China look extremely risky going forward.

At the same time the Chinese Yuan has reached its lowest level since 2008.



The Chinese debt problem will cause something to break.



## An Update on Ark

It's been a few months since we mentioned Ark Investments and Cathie Wood. After all, not much to report on when a. you are not investors and b. the funds are getting trounced. If negative returns were the goal, Ark would be doing laps over everyone. Over the last week, two major news pieces dropped from Ark that we found interesting and decided to share.

Cathie Wood has stepped down as Portfolio Manager from.....2 Ark Investments funds. We also for a brief second thought "could this be it for Wood?". Wood stepped down from the ARK 3D Printing ETF (PRNT) and ARK Israel Innovative Technology ETF (IZRL). Ark has over 10 ETFs and Wood remains the Portfolio Manager on the rest of Ark's funds.

The funny part is Wood stepped down from two of the better performing ETFs this year. ARKK is down 60% YTD while PRNT and IZRL are down 40-45% YTD.

William Scherer will replace Wood as the Portfolio Manager for both funds.

After those announcements, only a few days passed before Wood and Ark were back in the news.

MARKETS

## Cathie Wood's new fund gives small investors access to the VC market for just \$500

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Their long-awaited publicly traded venture capital fund is launching which will give individual investors exposure to private early-stage technology investments. The idea is good as retail investors do not get exposed to these investments due to the minimum capital required to invest. The ETF will expose investors to 70% private firms and 30% public. Investors will be able to buy the ETF on a trading platform Titan which is backed by venture capital giant Andreessen Horowitz (which seems kind of fishy).

"We are doubling down on innovation," Wood said in an interview Tuesday on CNBC's "Squawk Box." "Ark is moving from social media and social marketing into social distribution, direct to consumer. Pretty exciting. We are offering investors something they've not been able to access before." Wood has long stated that she prefers private markets as there is less volatility, perhaps she has forgotten that most early-stage technology investments fail. We will leave that to her to figure out. She just thinks she will be more successful in private markets as her holdings are not marked to market every minute.



The biggest piece of news regarding her Venture ETF is the fees associated with the fund that investors will be paying annually..... Ark's venture fund will charge a flat management fee of 2.75% and does not charge any carried interest or load fees. The total expense ratio of the fund is estimated to be 4.22%.

A 4% management fee is absurd. The best hedge funds in the world do not charge that. Typical venture capital funds charge 2% management fees and a 20% share of profits. Yes profits could make that management fee larger than Wood's but at least there is a major incentive. Wood's funds are down 60%+ YTD, who is going to pile into this when she's charging that high of a fee that is guaranteed to her? Our advice: cut fixed costs and drop your management fees to help small-time investors that you are trying to help.

For now, we will pass on this new fund, who knows maybe one-day companies that trade at 50x Sales can return to their 100x Sales peaks and ARKK will roar.

## European Central Bank

In Europe, there is no such thing as quantitative tightening at least this year. Over the last week, the ECB Balance Sheet grew by more than \$20 billion. The ECB Balance Sheet is now equal to 81% of the Eurozone's GDP compared to 35% in the U.S.

While the situation is bad in Europe, it is much worse in Japan where the Bank of Japan's balance sheet is equal to 128% of the country's GDP.



The moral of the story is easy money inflated asset prices not only over the last 3 years but the last 10 years. Imagine if these Central Banks offload their assets to 2016 levels? The ECB Balance Sheet quadrupled from 2015 to 2020. The ECB has finally begun talking about tightening its Balance Sheet but do not expect a policy change anytime soon.

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Either way between inflation, Central Bank policy, and an energy crisis, Western Europe seems in peril. These issues could potentially lead to another debt crisis in the region. The "most forward" thinking countries in the world continue to make some of the worst decisions. Perhaps, they can learn from mistakes but usually, these leaders just repeat them repeatedly.

Right after we wrote this piece (literally a few hours later), the Bank of England announced that they would begin purchasing long-dated English bonds to stabilize the market. The Bank will start buying government bonds at an "urgent pace" to help restore "orderly market conditions". This news came as the British pound hit a new low on Monday.

UK yields immediately dropped in reaction to this decision.



The first country to blink on quantitative tightening and interest rate hikes was England. We knew the pause would be soon, we had no idea it would be this soon. The Bank of England will lead the way and the FED will follow their lead in quantitative easing. Rising rates and financial markets in distress are currently political nightmares. Powell and the FED could be forced to change path in their next policy announcement which is coincidentally a week before the midterm elections.

For now, we leave you with an image from Zerohedge.



### A Bank with some Backbone

Last week the CEOs of the major U.S. banks testified in Congress. As usual, they got drilled by both sides. Democrats called them greedy, dangerous, and too powerful and Republicans woke, activists, and were dangerous to America. Typical Congressional Hearing.

There was one interesting headline we read from the hearings.

## **Dimon Defends Need for Fossil-Fuel Investments to Congress**

Jamie Dimon of JP Morgan defended fossil fuel investment by his bank, proclaimed the need for more investment in the sector, and would not promise to stop investing in the fossil fuel sector. For years most banks shunned investments in the traditional energy space and bowed to their largest shareholders. It seems Jamie Dimon might personally have a large exposure to energy, or his bank has increased its position.

As the tide turns, we are glad to be on the front end, when the tide turns over, the energy sector will be steaming full speed ahead. Even though energy stocks have erased large portions of their gains in a matter of weeks, the sector still has its best setup in the year due to the fundamental problems across the sector. The problem will only get worse and has not been addressed as the sector continues to be attacked by politicians.

Even with a recession, extreme economic pessimism, rising interest rates, and a bear market, oil is still trading near \$80/bb. The recent price movements have been more about market volatility and fear and less about fundamentals. The setup has not changed whatsoever.



Even though short-term volatility will continue, long-term fundamentals remain intact. Goldman Sachs seems to agree with that thought after releasing the economic research on oil pricing this week. They cut short-term price projections but also recommended long-dated oil exposure.....



## Oil

### Demand concerns mask unresolved underinvestment

- Despite outperforming cyclical assets this summer, oil prices finally succumbed to rising growth concerns, back to their lowest level since January. A strong USD and falling demand expectations will remain powerful headwinds to prices into year-end. Yet, the structural bullish supply set-up - due to the lack of investment, low spare capacity and inventories - has only grown stronger, inevitably requiring much higher prices.
- Updating our supply, demand and pricing models, we still end up on the bullish side of this quandary. This reflects our estimate that - at our supply expectations - current prices reflect zero real global GDP growth in 2023 outside of China, roughly 2 p.p. below 2023 consensus expectations, alongside range-bound Chinese oil demand for the coming year. While it may be surprising that oil is pricing such low growth expectations, this reflects the outsized exodus of investors, forced away by the extreme price volatility this spring.
- We acknowledge the ongoing growth slowdown, and, as a result, now base-case global GDP growth outside of China of c.1% in 2023, simplistically anchored at the post-war average weakest years of economic growth prior to 2008. This is a cautious assumption, below consensus expectations, while in China, we expect that zero-Covid policies will remain in place through next summer. On the supply side, we continue to expect that Russian supply will decline into year-end when the EU embargo kicks-in alongside the end of the globally-coordinated SPR release. Based on these updated views, we still expect a seasonally adjusted global oil market deficit in 4Q22 and in 2023, taking account of builds required for demand growth and for the redirection of Russian oil.
- As a result, from the current depressed level of positioning and prices, we reiterate our bullish price view, although our weaker demand growth expectations leads us to revise our 2023 forecast lower by \$17.5/bbl on average. At our updated assumptions, it would take an economic hard-landing to justify sustained lower prices. While we acknowledge that the short-term path to prices is likely to remain volatile, with the USD in the (opposite) driving seat, we find our conviction in the long-term bullish view only reinforced by the ongoing global supply disappointments. We recommend initiating a Dec-24 long Brent position.

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