

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.*



Boca Grande Lighthouse, Florida



Gibraltar Point Lighthouse, Toronto, Canada

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



China Moves On

As the world moved past Covid-19 and began to treat it like the common cold or the flu, China continued to enforce the zero Covid-19 policy. Up until a few weeks ago, the Chinese economy has been under consistent lockdowns due to the strict policy the CCP was enforcing regarding Covid-19.

Entire buildings were locked down if one resident tested positive, people were dragged to Covid-19 camps, and businesses were forcibly shut down. The entire process seemed draconian and overkill and even when the world moved on, China seemingly doubled down on its policy. They have even reportedly edited their domestic broadcast of the World Cup to hide fans in stadiums not wearing masks. Why did they do this? Perhaps another way President Xi could show his people and the world that he had ultimate power. We mention all this because China is opening, and their state media have reported that it is time to treat Covid-19 like a cold. We are glad the CCP figured out what the world has known for over a year.

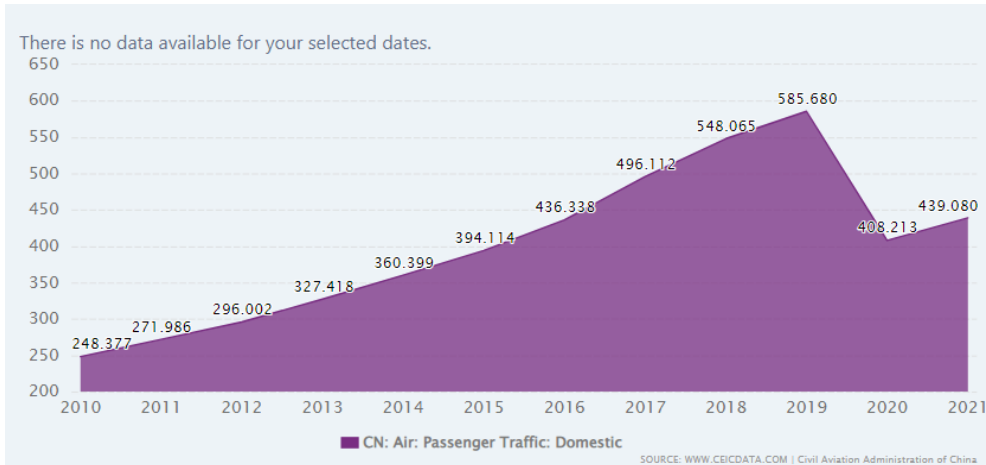
Why does this matter? China shut down production in manufacturing facilities across numerous industries when enacting its Covid-19 policy. Companies that had a reliance on China were essentially at the whim of President Xi and his authoritarian rule. With this shift in policy, commodity demand will begin to pick up moving forward. China is the world's largest manufacturer, and the demand for oil, gas, coal, copper, silver, and many other commodities will increase as China officially reopens. Global policymakers probably had a smile on their faces when they read this story. Many believe this move by China is extremely bullish for the global economy. This comes at a time of serious economic uncertainty across the world.

Chinese consumers took the news well and flocked to booking sites.

China Air Travel Demand Surges as Covid Zero Rules Dismantled

- Thousands of flights added daily as travelers return to skies
- Lunar New Year bookings jump in boon for loss-making carriers

A nice increase in fuel demand over the next few months is yet another bullish market fundamental in the energy market. Perhaps a return to pre-Covid-19 flight activity is on the horizon for China.



Flight activity has yet to return to pre-Covid-19 levels and with years of lockdowns, the demand could be greater than ever in the coming months to a year.

In 2019 China was the largest consumer of energy across the world, and as supply is not improving across energy markets, China's reopening could drastically increase global demand for oil and gas.

World Primary Energy Consumption per Capita in 2019

Country	% of world population	% of global consumption
China	18.47	24.27
India	17.70	5.83
Africa	17.2	3.40
Europe	9.59	14.36
United States	4.25	16.21

The setup in energy which was already quite green seemingly improved yet again this week. Hopefully, November and December's drop in energy prices did not scare you away. Nothing of consequence has changed.



November's CPI Dump

Inflation, inflation, inflation. That might be the word of the year for 2022. Consumers have felt the pressure of rising prices across most things they have bought in 2022 and investors have seemingly weighed every decision on inflation data.

We feel for consumers and believe that external pressures have led to price increases (companies for the most part are not expanding margins), some of which could have been avoided but some that could not have been. Supply shortages have led to higher prices, but the causes of those shortages have not been addressed and have been glossed over by governments and companies (this could cause inflation to stay high for years to come). In summary, companies and governments are screwing up and consumers continue to foot the bill.

On Tuesday, we got our last Consumer Price Index release in the 2022 calendar year. CPI dumps have been highly anticipated in 2022 and have impacted investor decisions more than ever. The CPI for November came in at 7.1% down from 7.7% the month prior and lower than analyst expectations of a 7.3% increase in prices. Many have signaled that this officially confirmed inflation has peaked and we are on our way down.

We think that inflation has peaked in the short to medium term and that inflation numbers will retreat moving forward. However, we do not think that it will be a straight line down and it will not be a quick ride back to the 2% level that most Central Banks target when it comes to inflation. More on that later.

Investors took this CPI print very positively and believe that this could cause the FED to pause their interest rate hikes in the coming weeks to months.

Core CPI rose 0.2% on the month and 6% on an annual basis, compared with respective estimates of 0.3% and 6.1%. "Cooling inflation will boost the markets and take pressure off the Fed for raising rates, but most importantly this spells real relief starting for Americans whose finances have been punished by higher prices", said Robert Frick, corporate economist with Navy Federal Credit Union.

Energy prices declined 1.6% for the month, due in part to a 2% decrease in gasoline prices. Food prices, however, rose 0.5% and were up 10.6% from a year ago. Even with its monthly decline, the energy index was higher by 13.1% from November 2021.

The CPI lowering is a good sign but what happens when energy prices tick up? Energy prices are up 10-15% over the last year, well below their peak levels from the spring and summer. Prices have dropped recently but could be on their way back up. Winter is here and its cold which will lead to a surge in demand, the Strategic Petroleum Reserve (SPR) also looks like its drying up (the SPR is at its lowest level since 1984 and has decreased in size by over 30% in 2022), and OPEC is not offering any assistance in terms of increasing supply. This could lead to an increase in energy prices and ultimately a resurgence in the CPI.



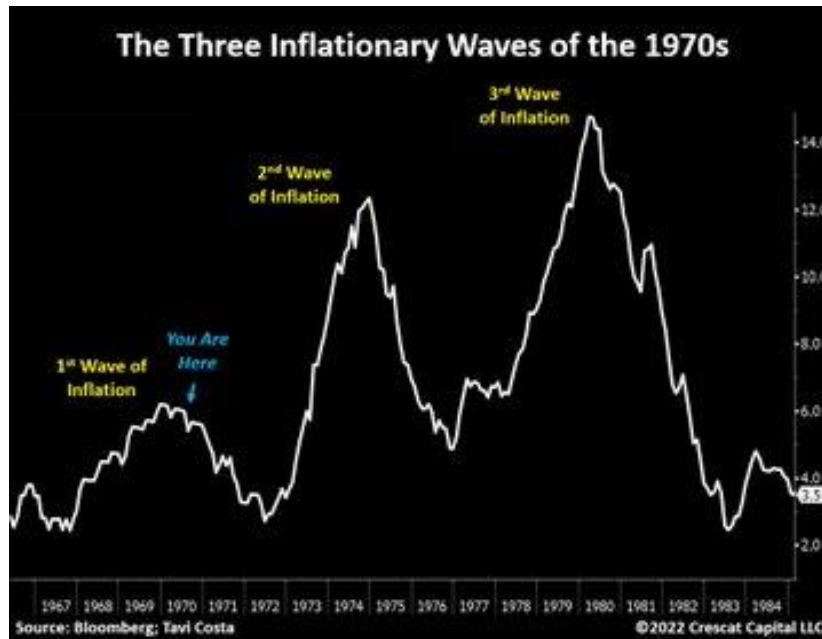
The one thing that we know that has peaked is used car prices. Used cars surged in price during Covid-19 due to chip shortages, production delays, and manufacturing facility closures. With all that used car prices surged to record rates. Consumers were trading in their cars for more than what they paid for. The market was completely out of whack. Hopefully, you did not have to buy a car at this time because if you did, you are more than likely kicking yourself.



After looking at the recent CPI dump which is a summary of what has happened (in the past), it is important to look forward.

Statistics regarding the economy are for the most part backward looking. So how do you project prices? That is a complex process that we will leave to the Economists. We are Portfolio Managers.

Instead, we will look back at historical data for the last time inflation was high. Inflation surged during the 1970s and even though it decreased quite quickly during the original surge, it did not return to the 2% target for over 10 years.



So, it took the FED 10 years to reign in inflation, and even though they got it to decrease on numerous occasions, it surged higher shortly after. Perhaps we are in the early innings of a cycle that could have inflation peaking in the next few years.

Perhaps the 2020s will be quite like the 1970s in terms of inflation. The one thing we know that could remain elevated in price in years to come is food and energy prices. The policy has not changed to improve the supply of these necessary goods and regulation continues to increase across these industries. We expect energy and food prices to continue to move higher in years to come. Even if governments pivot and promote the increase in the supply of energy or even food, expansion takes time.

If commodity shortages continue and wages continue to grow, inflation in the 2020s will be a mirror image of the 1970s.

Even though we think inflation will continue for years to come (perhaps the next decade), we do think prices will cool down to start 2023. However, this does not mean the CPI will return to 2% like the FED and many consumers want it to.

Rising Rates, Bad for Governments too

As interest rates are hiked, consumers are being pushed to the edge, loan interest rates are increasing across the board which has affected consumers across the world. Mortgage rates are increasing at their fastest speed in over 10 years which has slowed down the housing market. Rising interest rates have also affected investors across debt and equity markets. Even though the FED has increased interest rates to combat inflation, they have also hurt itself in this process. As interest rates rise, servicing debt becomes more expensive, this increases the budgeted amount to pay back interest and in turn, cuts



government (or company) spending in other areas (or the government can create more money and in turn more inflation). By raising rates to combat inflation, they will be spending more to pay back debt from years prior. We say this because governments are the biggest debtors in the world, and they are going to begin to feel the real effects of rising interest rates. What gets cut first from government budgets? Health care? Education? Infrastructure? Defense? We are not sure, but it is something to remember. Whenever, you hear someone say the FED and the government will continue to raise interest rates and it does not matter how high they will go, show them this chart, and explain to them how this becomes a self-inflicted wound that could make today's inflation much, much worse.

Many people are looking past the glaring issues that face western governments. Every western country printed money and added on piles of debt for the last 50 years. However, most of that debt was added on in the last 15 years (post-Financial Crisis). Has this changed how governments approach policy? No, if anything it has made them promise more to voters by adding on more debt.



Free university, universal health care, free dental care, energy stimulus payments (for rising prices), higher wages for government workers, new energy sources, increased energy development investment, and increased military spending are mostly new phenomena that you seem to hear more about as time moves forward. New government promises are quite expensive. We are not advocating for any political party or stance on a major issue. We are simply stating that the U.S., Canadian, British, French, Japan, and every other western government has a debt problem. We again ask: what gets cut from budgets first to account for rising interest payment costs? It's a tough question that needs to be asked.

This phenomenon is also reasoning many investors think interest rates will begin to get slashed as the government simply cannot afford to service its debt at higher interest rates.

Interest payments will soon become a significant part of governments' budgets.

US Government Debt Spending Soars to \$103 Billion for Two Months

Over a 12-month period, debt servicing costs are estimated to be over \$600 billion at current interest rates. By 2025 or 2026, the United States may hit a bleak milestone: Federal interest payments could exceed the country's entire defense budget, according to Moody's Analytics. Interest payments will only increase in value as interest rates are hiked by the FED and other Central Banks.

Even China, a major U.S. creditor has noticed the added costs associated with debt as interest rates have risen.



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US debt hits record as cost to service it rises

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China, US agree to communicate, boost relations

Sam Bankman-Fried (SBF) Arrested Before Congressional Hearing

It's official, SBF or the CEO of FTX has officially been arrested. We are sure you know what happened and what has been happening over the last few weeks. The story is wild and continues to change. After weeks of living freely in the Bahamas, SBF was picked up by the Bahamas Police and will be held in the Bahamas without bail. The charges include wire fraud, wire fraud conspiracy, securities fraud, securities fraud conspiracy, and money laundering. SBF was arrested at the request of the U.S. government and the Department of Justice.



On Monday, SBF gave another interview, this time it was not at an elitist New York Times event, but at a Twitter space hosted by a large Financial Twitter account Unusual Whales. SBF was also planning on testifying (remotely) in the U.S. House where he would be under oath on Tuesday. Many point to his arrest timing as interesting, he was arrested just a few days after agreeing to testify.

We are not claiming conspiracy and are not claiming that his arrest will prevent the truth from coming out. We are simply stating that the public might not get any information for years to come. His arrest presents numerous problems, especially for certain politicians. SBF donated millions and potentially billions to politicians with money that was never his. Will politicians be forced to pay the money back to users who were essentially robbed? This is just one of the hundreds of questions that people want to be answered.

According to insiders and leaks, SBF was reportedly going to throw the blame at everyone but himself while testifying in Congress.

Members of Congress on both sides of the aisle showed their frustration at the FTX hearings and online after SBF was arrested. We do not blame them whatsoever. He stole billions to fund his lifestyle and his failing hedge fund.



Speaking of Crypto

The collapse of FTX was yet another nail in the coffin for cryptocurrencies. The industry that once had 0 regulation is being scrutinized more than ever (as it should).

This week, the Canadian government banned the use of crypto leverage and margin trading in response to FTX's collapse.



HELEN PARTZ

DEC 13, 2022

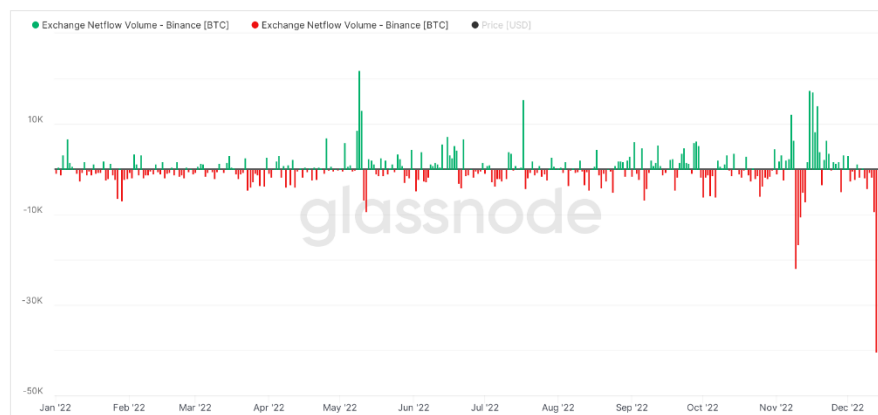
Canada bans crypto leverage and margin trading after FTX collapse

Now-bankrupt exchange FTX attempted to enter Canada in June 2022, but local regulators have managed to prevent the mess.

We are not claiming to be crypto experts but allowing crypto leverage seems extremely irresponsible. The asset is EXTREMELY volatile, and unregulated. This seemed like a recipe for disaster. Anything that lacks intrinsic value, that has an unpredictable future value should not be allowed to be used as margin or be allowed to trade with by using leverage.

The distrust of FTX also looks like it is leaking across the industry. Binance saw its largest withdrawals ever this week. Users pulled their Bitcoin from the platform out of liquidity fears. Perhaps users are realizing these new-age exchanges are not so secure. Security is critical on platforms that hold your assets but so are regulations and what they are doing with the funds that you have trusted them with.

Bitcoin: Net Transfer Volume from/to Exchanges [BTC] - Binance



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“CZ” the CEO of Binance said these outflows and other withdrawals could lead to a tough few months for Binance including potential layoffs.

Analysts believe that over \$6 billion in customer funds were withdrawn from the platform in just under 24 hours.



No matter how you look at it, the cryptocurrency industry remains unstable and will more than likely remain that way until something changes. It seems more and more consumers are realizing the fundamental pro of crypto is also a major con (limited supply available, unlimited supply of coin types). Thousands of coins worth absolutely nothing.

Finance Twitter Gets Hit

In this publication, we have written about the growing use of Twitter in Finance. In theory it is extremely useful, the ability to talk with thousands of people, share ideas, and meet new people and all with extreme ease. We explained that many responsibly use Twitter in the Finance industry (promoting commentaries, talking ideas, and sharing their respective thesis'), but highlighted the select accounts that were essentially partaking in pump-and-dump schemes by utilizing Twitter. It was essentially Wolf of Wall Street on Twitter and in Discord lobbies. It was glaring to us that something was illegal.

Essentially accounts with hundreds of thousands or more of followers would promote stock and constantly tweet that it was going to the moon. The stock usually did surge as their loyal followers were buying it up. What those followers failed to realize is these "influencers" were pulling the rug from under them.

After years of this behavior, it seems a select few people who run these accounts were hit with a massive suit.

SEC Charges Eight Social Media Influencers in \$100 Million Stock Manipulation Scheme Promoted on Discord and Twitter

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We do not know the particulars of this case but saw this coming from a mile away. People should not be able to manipulate a stock on social media and should not be getting their financial advice from a few fake accounts on Twitter.

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