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.

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.

Cape Blanco Lighthouse, *Port Orford, Oregon*

The lighthouse was built in 1870, making it the oldest standing lighthouse in Oregon. In 1980 the Lighthouse was automated and is now on the National Register of Historic Places.

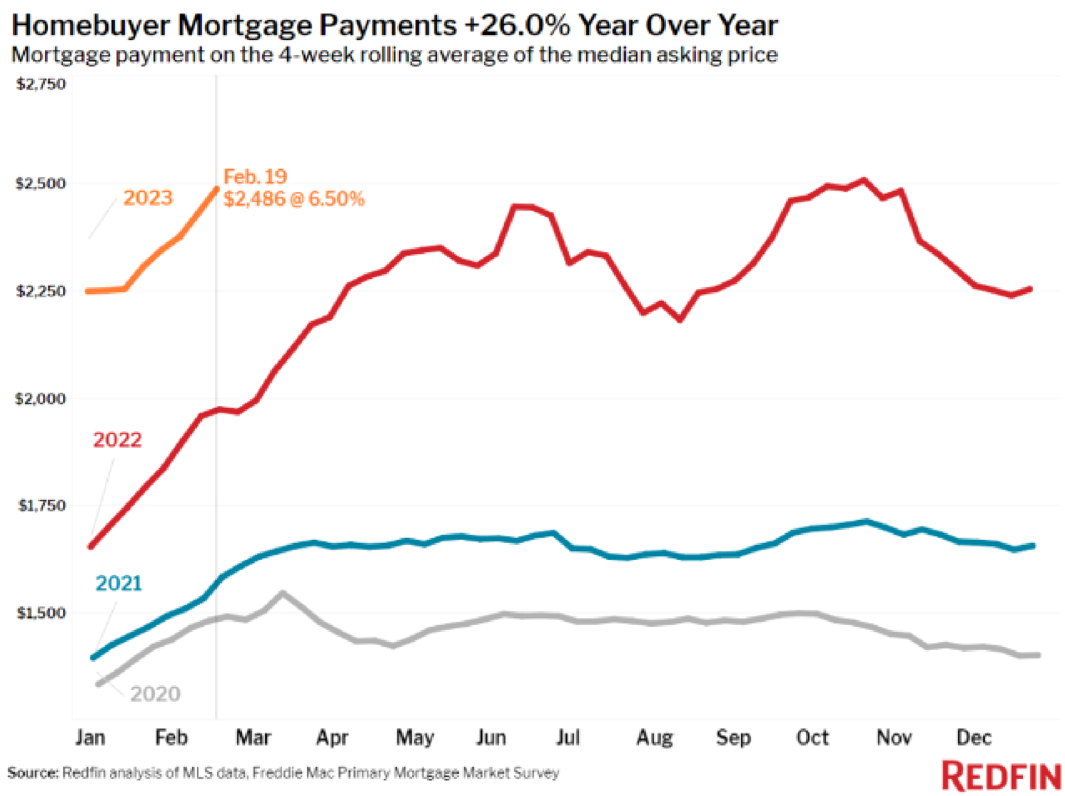
Point Cabrillo Lighthouse, *Caspar, California*

Point Cabrillo Light is a lighthouse in northern California, United States, between Point Arena and Cape Mendocino. The Lighthouse was constructed in 1909 and stands 47 feet tall. The Lighthouse has a range of 22 nautical miles.

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

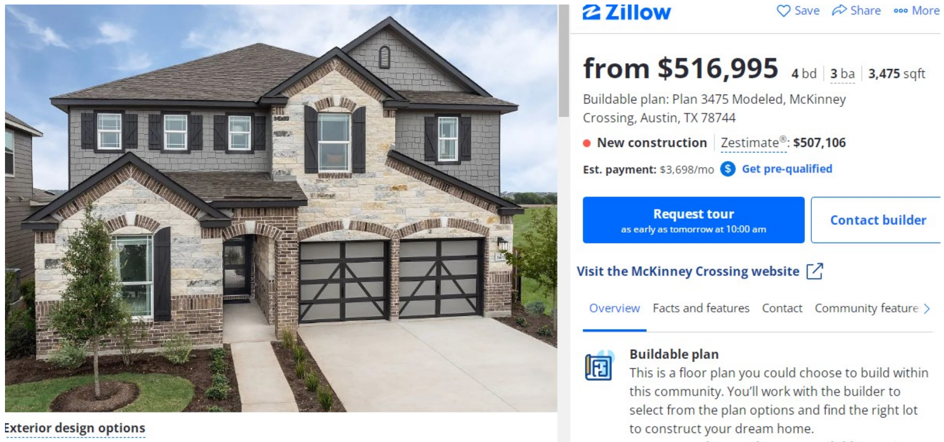
Residential dreams

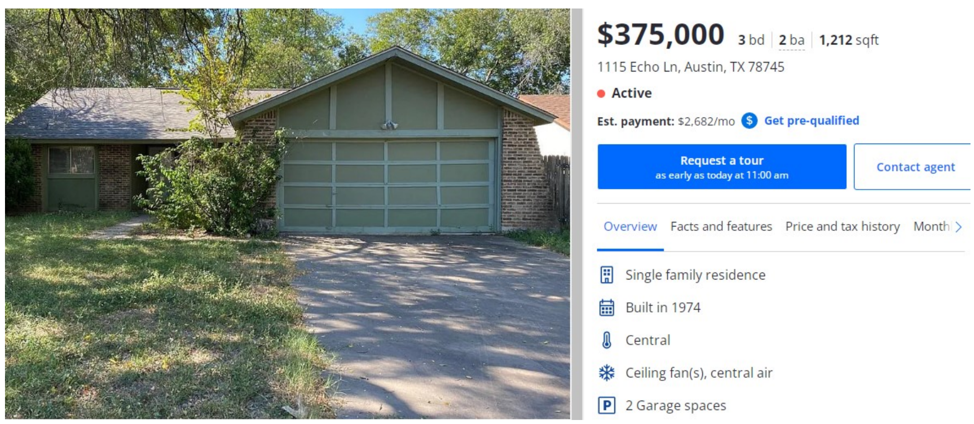
Mortgage payments continue to soar as interest rates hit 15-year highs.



Even though real estate prices have decreased in recent months, consumers are still paying a lot monthly due to high rates. The average U.S. mortgage payment is up 26% year over year. The average consumer is paying $2,486 per month for a mortgage compared to $1,500 in February 2020 (pre-Covid-19).

Due to rising rates, buyers are being squeezed out on what they could afford a few years ago. According to Redfin, a US homebuyer with a $2,500 monthly budget can afford a $384,000 home today versus a $518,000 home that the same buyer could have purchased back in 2021 at 3% interest rates. To put those numbers in perspective, here are two homes for sale in the Austin, Texas suburbs.

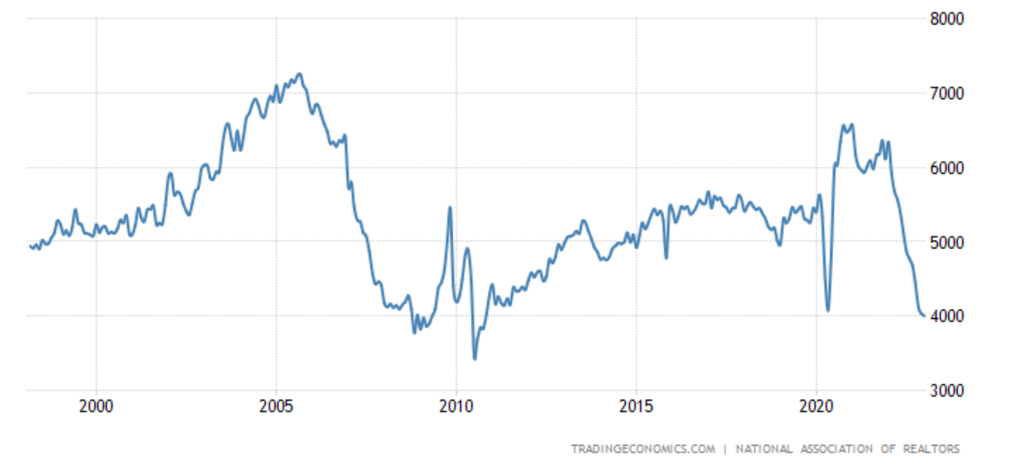




We are not making fun of the second home. We are simply illustrating the homes the same consumer can afford just two years apart. We do not expect a price reset in residential listings, especially in southern states. We think consumers will cut back on other expenses so they can stay in the market for their dream home. Consumers will stretch themselves as far as possible to afford their mortgage which could have deep consequences, especially in the long run if they face some sort of stress test.

Dropping prices could also impact sales volumes across the country as sellers are not getting close to what they think their home is worth (U.S. existing home sales have declined 12 months in a row). Existing home sales are at their lowest level since 2010 fueled by decreases in the Northeast and Midwest.

United States Existing Home Sales per month:



The real estate market (holistically) is at Covid-19 lows and is approaching Financial Crisis and not many people are talking about it.

A nightmare

WeWork has been a disaster for years.

The idea which originally seemed interesting eventually became a disaster. WeWork is a company that offers shared office space to individuals, and companies.

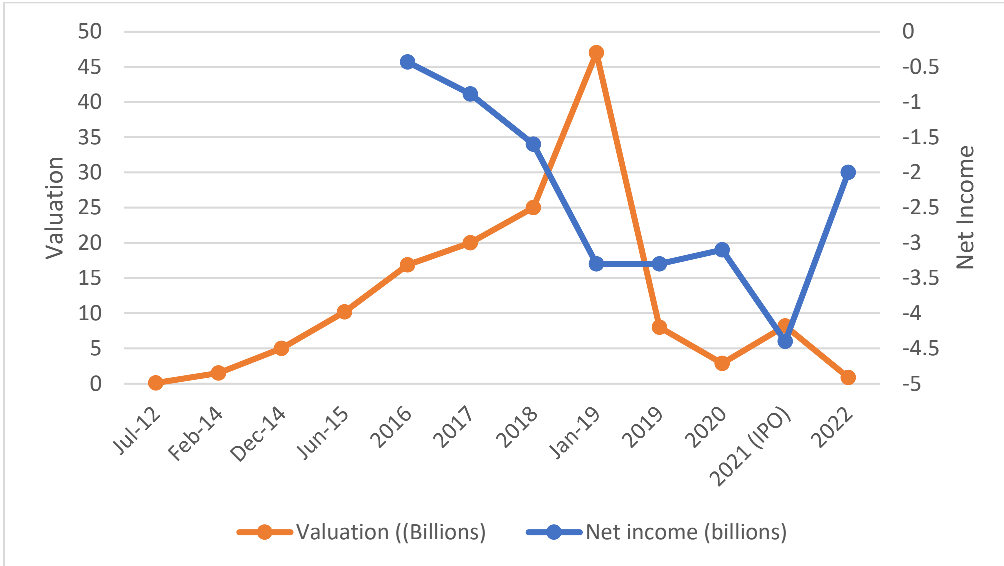
WeWork grew from a start-up to a multibillion-dollar enterprise in the matter of years. WeWork's main goal was growth. It made them a huge success in their early days but eventually became their Achilles heel down the road.

WeWork had a number of other issues that contributed to their downfall including the ridiculous valuation which was fueled by SoftBank and investment banks, an irrational founder, and an overestimation of their market. WeWork bought and leased billions of $ in real estate, betting on a market that 1. Did not exist and 2. That was shrinking.

The company has burned through cash since being founded and has yet to turn a profit. The company has historically put growth first, and profitability second.

WeWork's combined net income since 2016 is -$15.7 billion.

WeWork's peak valuation was close to $47 billion, today its market cap is below $1 billion. Imagine participating in an investment round when the company was worth $20 billion+. We assume those that did are questioning their due diligence process. Here is WeWork's valuation and net income over the years. WeWork was founded in 2010.



Numerous news outlets reported that investment banks pitching WeWork in mid-2019 were using valuations in the $60-100 billion range to impress founder Adam Neumann.

WeWork went public via SPAC at a reference price of $10/share in October 2021. Shares have collapsed to $1.12 since.

WeWork's founder has an estimated net worth greater than WeWork's market cap as he was pushed out of the company at a much higher valuation.

WeWork is a glaring example of why continuous growth with no care for profitability is a dangerous business strategy. We hope you did not invest.

Although WeWork had the biggest relative collapse in value from its peak, it is not alone in the world of unprofitable, growth at all costs, collapsing new-aged companies. These companies ballooning in value was due to a combination of hype, retail traders, and easy (cheap) money. They promised all kinds of things and have yet to deliver.

Electric vehicle maker files for new raise

Auto production is capitally intensive. Creating a supply chain and scaling production is difficult. The industry has high barriers to entry due to capital requirements. The EV world might be even harder to enter due to technology and the ability to source inputs. We have regularly said that many of these new EV companies will burn through cash as they scale. Some of these companies may go bankrupt or could be bought out over the next few years.

This week, electric vehicle producer Rivian announced plans to raise $1.3 billion in a convertible senior note issuance that will mature in 2029.

Convertible notes offer investors the security (and interest payments) of bonds while also giving them some upside in the performance of a company's stock. Purchasing a convertible note is almost like buying debt and a stock option all at once.

Even though Rivian had $12 billion in cash on its balance sheet to the end of 2022 which is enough to fund operations for a few years, Rivian will need to eventually raise billions as analysts do not forecast any profits until the end of the 2020s. Rivian's revenue grew from $55 million in 2021 to $1.65 billion in 2022. Rivian's net income was -$6.75 billion in 2022 and -$4.69 in 2021.

Rivian shares dropped more than 11% on this announcement, reaching a 52-week low. Rivian shares have dropped 88.4% since their IPO in November 2021.

Despite the collapse in the company's market price, Rivian still has a market cap of $14 billion.

Perhaps, Rivian becomes a serious competitor to Tesla in the EV space moving forward and eventually become profitable, but they could also continue to burn cash for the next decade. We are not sure which way things will go, especially for a company that is early in its production life. Rivian delivered 20,000 vehicles in 2022 (to put things into perspective, Tesla sold 1.3 million units in 2022). The only thing that is certain for Rivian is that they will need to raise billions over the next 3-5 years to support operations which will dilute their current shareholders.

New World

Ford filed a patent that would allow the company to cut off a customer's air conditioning or radio in their automobile if they are delinquent on a payment.

The patent could even lock vehicle owners out of their vehicles until a payment is made. Ford says it does not plan to use these features but is filing patents for these features along with others.

This would protect auto companies against delinquent borrowers but opens a serious can of worms for the industry and other industries. Will banks do the same on your house for mortgage payments (ie. Locking you out, or turning off features)? How about landlords flipping the switch on electricity or your oven due to late rent? We are not promoting delinquencies, just pointing out the issues with this new technology.

No matter how you feel about this technology, it is something interesting to follow moving forward. We expect legislation to eventually be put in place to protect consumers in extreme cases.

FTX update

SBF (Sam Bankman-Fried) and FTX, are two 3 letter acronyms that have done tremendous damage. BTW, a quick Google search refers to SBF as an "American entrepreneur".

While SBF awaits trial, a bankruptcy firm is liquidating FTX and looking at where all the money went. According to them, FTX can only account for $2.6 billion in customer deposits but is currently responsible for $11.2 billion. The company currently holds $6 million in Bitcoin for customers, yet it is responsible for $1.591 billion in Bitcoin. The same is true for Ethereum and many other assets which customers thought they owned.

The story is horrible. The money discussed above is purely customer money and does not include investor capital provided to FTX to grow the company.

One of the more notable numbers is an Accounts Receivable (money owed to) entry for $12.8 billion from Almaeda Research. Yes, SBF loaned his failing hedge fund almost $13 billion. So how did Almaeda lose that money? They made high-risk, leveraged trades to try and gain back lost money and kept losing more.

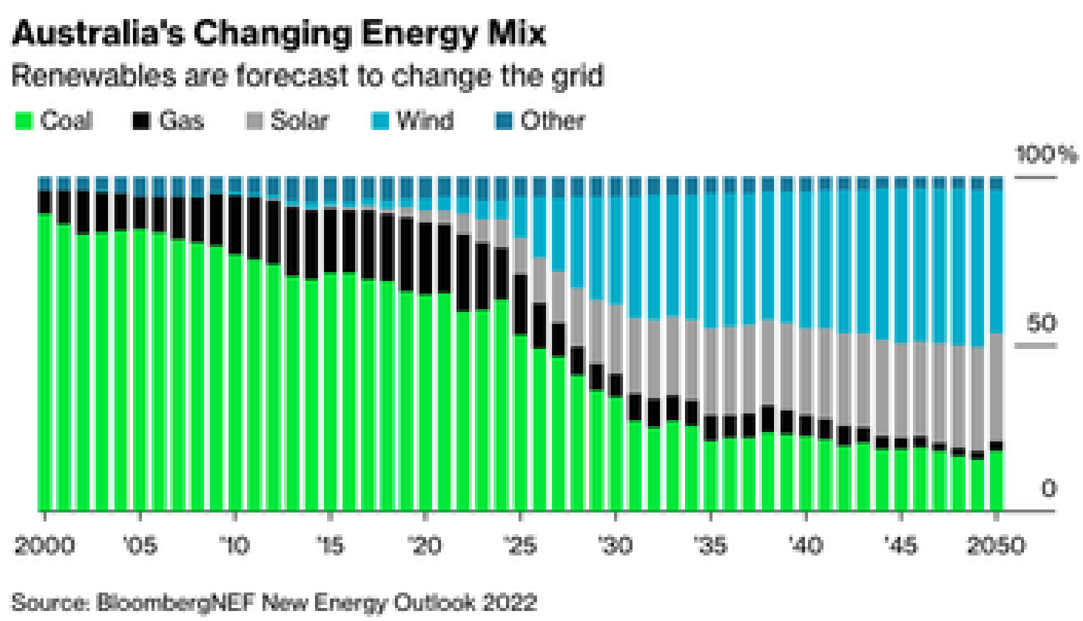
The major change since the last data dump by the bankruptcy lawyers is that they located an additional $638 million.

This is not the end of the story for SBF and FTX. We were not investors or users but will continue to follow the story up until its conclusion and hope regulators protect users over companies.

Aussie rules

Over the last 20 years, Australia has heavily leaned into green energy. They have invested billions and are still heavily dependent on fossil fuels. Currently, over 80% of their energy comes from fossil fuels.

Australia's net zero plans require them to continue investing in renewables and over the next decade rapidly decrease their dependence on fossil fuels. This will lead to higher prices for consumers. Electricity bills will increase in price and blackouts will become more frequent.



Expansion of wind & solar along with thousands of miles of new power lines could cost Australia over $160 billion USD.

Hopefully, they keep some of their coal mines in operation just in case of an emergency……

Governments lead the way

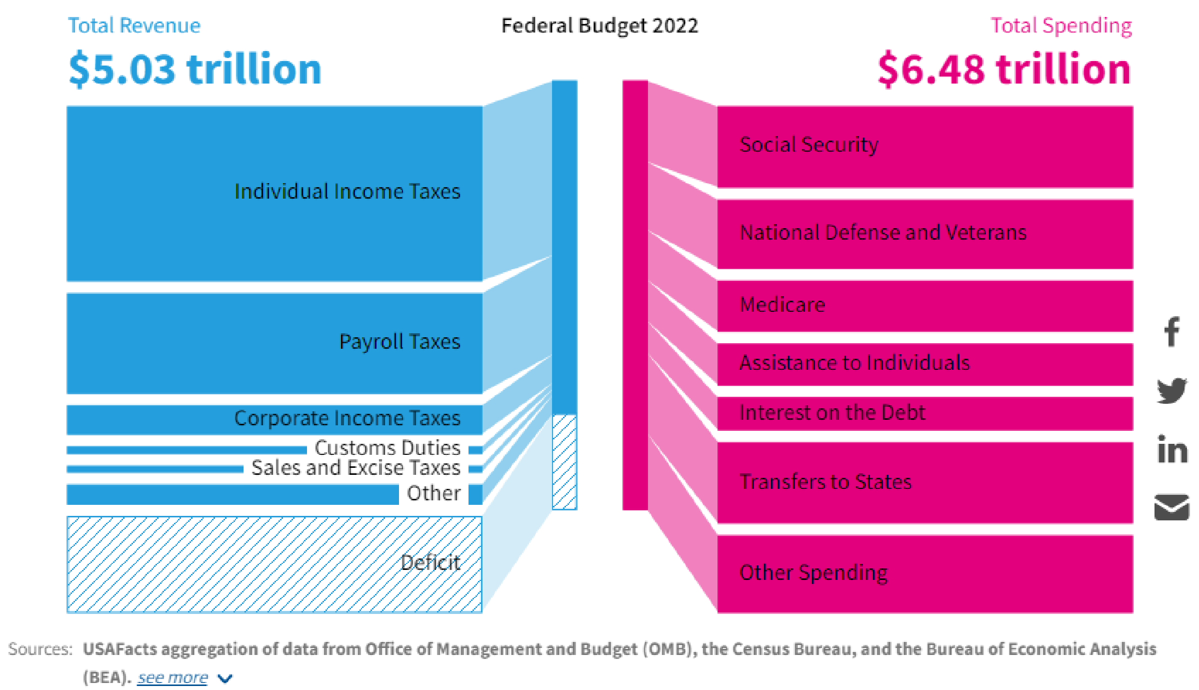
We often rip on companies that burn through cash. We think positive and strong free cash flows are essential when stock picking.

However, being unprofitable has become the norm for public companies over the last 5-10 years. Analysts and banks justify it by forecasting major growth. While some companies did eventually turn that corner through scaling, many have not. Many technology companies have burned through billions and have no road to profitability yet sell-side research analysts still place lofty forecasts on these companies. It's a double-edged sword as banks need investors to buy what they cover so they can collect their commission on a future debt or equity raise from said company.

We mention all that because one organization started this trend. One major organization made it acceptable and sexy to burn through cash and spend more than you have.

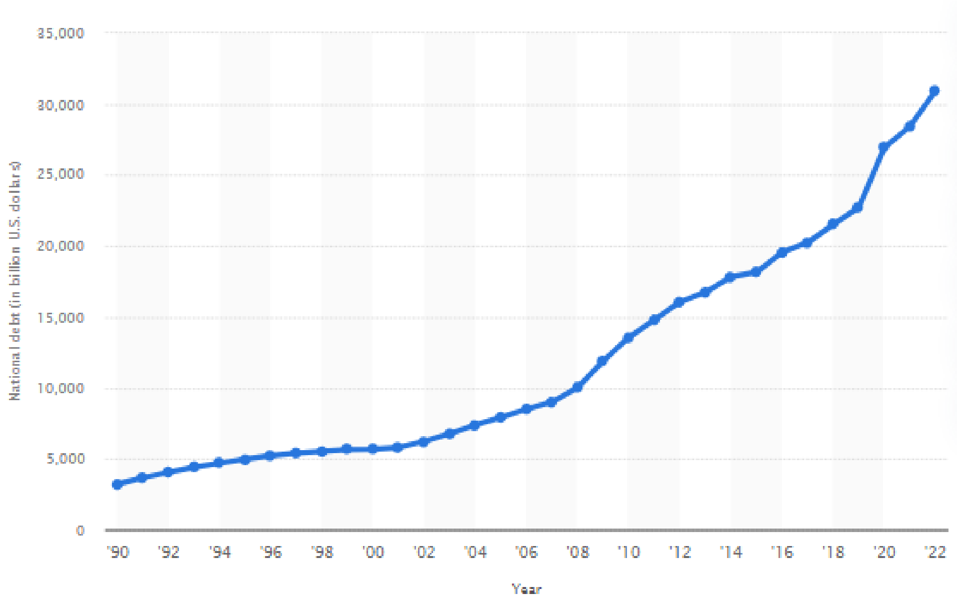
That organization is the U.S. Federal Government. Obviously, most western nations are doing the same thing, but the U.S. is the most powerful country on Earth and has arguably been the most powerful since the end of World War II.

To illustrate what we mean, look at this chart we ran across this week:



The government spent $1.45 trillion that it did not have. The U.S. continues to add on debt every second. The U.S. outstanding debt sits at $31 Trillion as of this writing. The U.S. National Debt has tripled since 2008/2009.

The U.S. Outstanding Debt since 1990 can be seen below:



2008/2009 was the moment the U.S. government decided it could not let its system fail. They created easy money printing billions to bail consumers and corporations out. This has continued since 2009. The government has created a safety net for everyone.

As interest rates dropped over the last 20+ years, servicing debt never became a major expense for the U.S. government. This allowed the government to add on more debt and spend more. As rates have increased over the last year, interest payments for consumers have increased substantially, and they have also increased for the government.

Analysts believe the cost to service outstanding debt could reach $550 billion in 2023, a large jump from last year. That might not sound like much, but it will continue to increase if rates continue to rise and remain elevated for the foreseeable future. You also need to contextualize $550 billion versus what the U.S. government spent last year, $6.5 trillion. That would account for over 8% of the federal government's budget. The government spent $750 billion on Medicare in 2022 and many are projecting that servicing that debt will surpass Medicare spending over the next few years.

Here are a few other major areas the U.S. spent money on in 2022.

Retirement	$1.03 trillion
Defense spending	$759 billion
Stimulus payments	$53 billion
Transportation	$36.5 billion
Transfer to states	$1.21 trillion
Public health	$140.8 billion

The federal government’s budget of $6.48 trillion equates to $19,434 per American. 52% of the government’s revenue came from individual income taxes in 2022.

Perhaps these high-growth and revolutionary technology companies that burn through cash are just following in the footsteps of Uncle Sam.

The trend of deficits and debt being added on will continue moving forward. The debt limit will once again be raised so the federal government can continue to operate. The U.S. is approaching its debt ceiling and is months away from being unable to pay for its obligations and budget. In order to raise the debt ceiling, you need Congressional approval. House Republicans have claimed they are willing to allow the government to default to get what they want.

This is all the more reason to own Alternative Assets (aka Real Assets) like private real estate, private equity, hedge funds that run counter to public investments and other hard assets like physical gold, silver and platinum. Real assets offer the opportunity for diversification, inflation hedging and competitive total returns. Real assets may also serve as a non-traditional source of income, a feature that investors frequently overlook.

What are the benefits of real assets in a portfolio?

Real assets **provide portfolio diversification**, as they often move in opposite directions to financial assets like stocks or bonds. Real assets tend to be more stable but less liquid than financial assets. As always, reach out to us for a better understanding of how this all works in a portfolio in today's challenging environment.

MacNicol & Associates Asset Management
March 10, 2023