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.

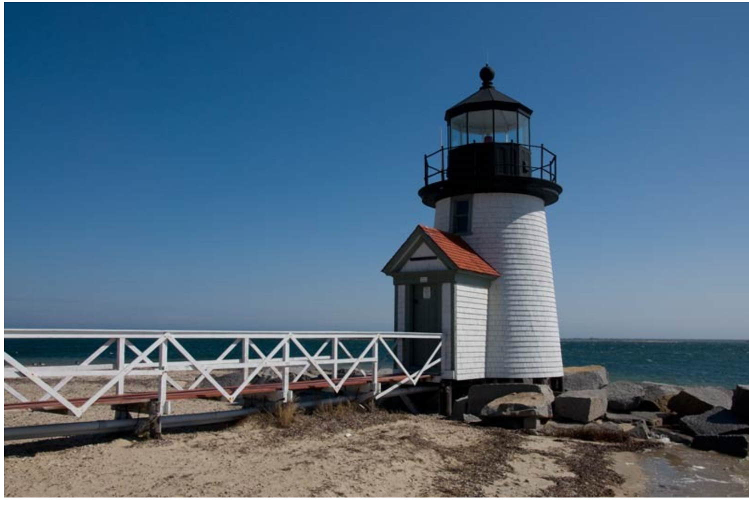
Contact us today if you would like to meet about your investment future. info@macnicol.com

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.

Beavertail Lighthouse,
Jamestown, Rhode Island

This lighthouse was originally built in 1749. Its current structure was built in 1856 at 64 feet tall. Over the past decade, different parts of the Beavertail Lighthouse station have been restored and the Museum received a large expansion.



Brant Point Light, *Brant Point, Nantucket, Massachusetts*

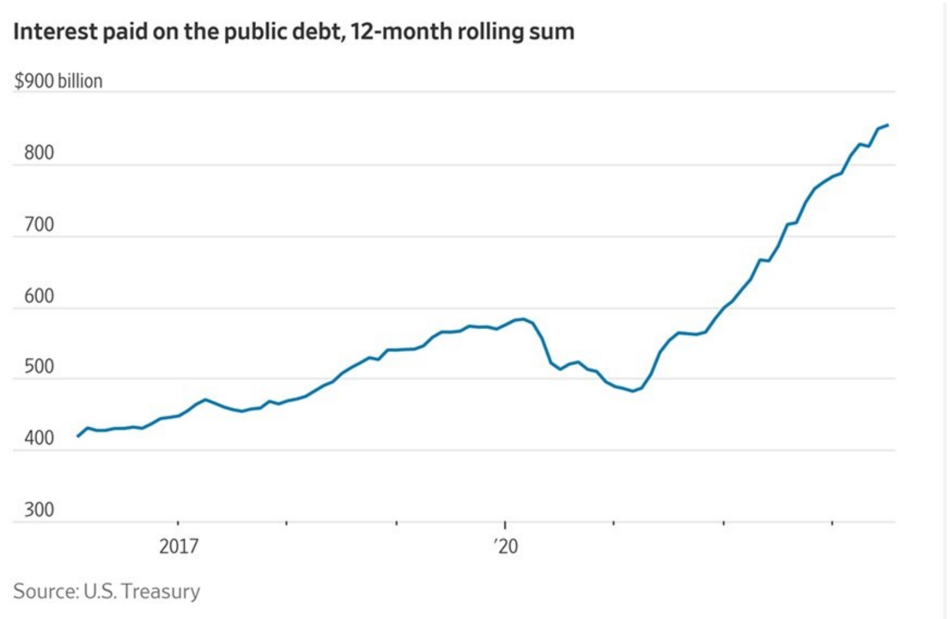
A brick tower was built at Brant Point in 1856 and is still standing but was deactivated in 1900. The 1856 lighthouse is still used as the Nantucket Coast Guard station. In 1975, Brant Point Light was added to the National Register of Historic Places.

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

U.S. government and interest rates

The Federal Reserve and Jerome Powell have hiked interest rates to 20-year highs, which has led to higher costs for consumers, corporations, and investors. The other entity that has also been negatively impacted by higher interest rates is the U.S. Federal Government which are the largest borrowers in the world.

The U.S. government has paid close to $850 billion over the last 12 months in interest payments. The interest they have paid on their outstanding debt is expected to increase over the next few months especially if rates remain elevated to start 2024.



The trailing 12 months of interest payments is more than double the 2018 number due to a higher FED funds rate and a higher outstanding debt value. The U.S. government has exponentially grown debt over the last 10-15 years. Most countries around the world have a similar problem and are over-leveraged. Governments have used trillions of dollars to bail themselves out of tough situations (Mortgage Crisis, Covid-19, Inflation). The leverage added on by countries eventually led to the inflation that we saw in 2021 and 2022 leading to interest rates being hiked to their highest point in over 20 years. The government essentially has created this problem, and there is no major solution unless it pulls back on its spending (something extremely unlikely to happen).

In order to illustrate the magnitude of the interest paid (approximately $850 billion) over the last 12 months on public debt, we found some relatively similar numbers.

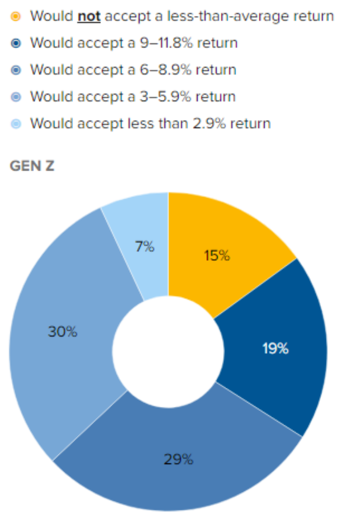
- In 2021 the U.S. government spent $797 billion on health care, less than the cost to service public debt (over the last 12 months).
- Tesla's market capitalization is $813 billion, less than the cost to service public debt.

- Switzerland had the world's 20th largest economy by GDP in 2022. The country produced $807 billion in output - less than the cost to service U.S. public debt.

The numbers are staggering. The story jumps off the page. The U.S. is hurting themselves by 1. Adding on more debt and 2. Raising interest rates. (We know Central Banks in most countries are independent entities and operate without government guidance. We are simply making an overarching point, as they are both public arms.)

Would you sacrifice returns for ESG?

CNBC recently released the results of a survey that has us raising our eyebrows. The survey suggests most young investors would accept returns lower than the S&P 500 if those smaller returns were invested in ways that match their values. A staggering 85% of Gen-Z investors said they would accept a lower return than the S&P 500, and 7% of them said they would accept a return of less than 2.9%.



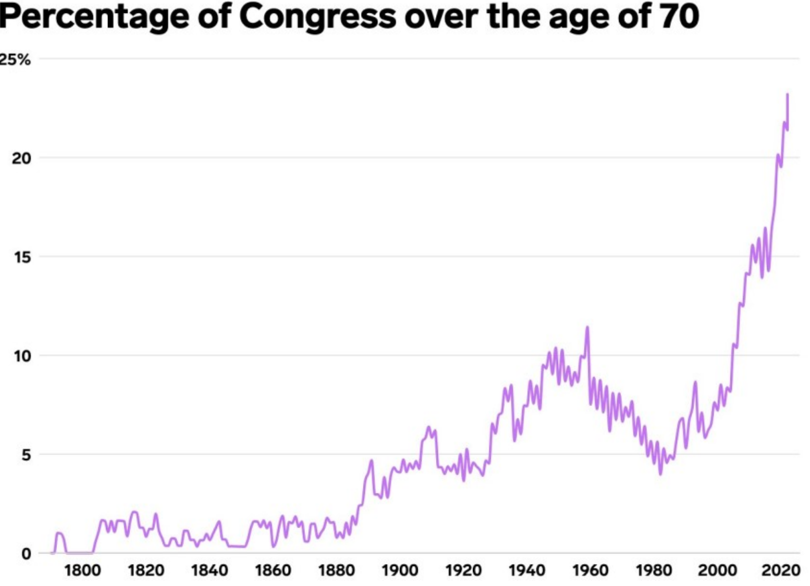
The survey done by U.S. Bank only includes "active investors".

Many of the investors surveyed pointed to companies putting their money where their mouth is (in terms of ESG actions), renewable energy solutions, water purification, and strong corporate governance as major drivers in their investment process.

The survey shed major light on how young investors want to be serviced and what they prefer. The survey also looked at older investors who were much less likely to sacrifice returns in the name of ESG scores. Perhaps this light will shift how asset managers, financial advisors, and institutions market and sell to young investors moving forward.

Exponential growth

A user on Twitter (X) created a graphic this past week that illustrated a problem that the U.S. is currently facing. We say problem very loosely.



Close to 25% of Congress members are currently over the age of 70, a record number. Just 23 years ago the number was just a tick above 5%. We know life expectancy has improved over time as modern medicine has improved, and health care has evolved, so we understand why the number was very low from 1800-1950. We are simply asking a question, why has the number of politicians above 70 years old quadrupled since 1980?

In 1980 the U.S. life expectancy was 73, and in 2020 it was 77.3, a slim jump over 40 years while the chart above jumped exponentially. So why are there so many older (and long-tenured) members of Congress?

We think it could have something to do with power (which most politicians crave) and enriching themselves, and their friends and families.

We have long tracked the abuse of insider information by politicians who shoot the lights out relative to indices. Why would these politicians retire if they can keep going? It seems like a win-win situation for them, more power, more recognition, and generational money.

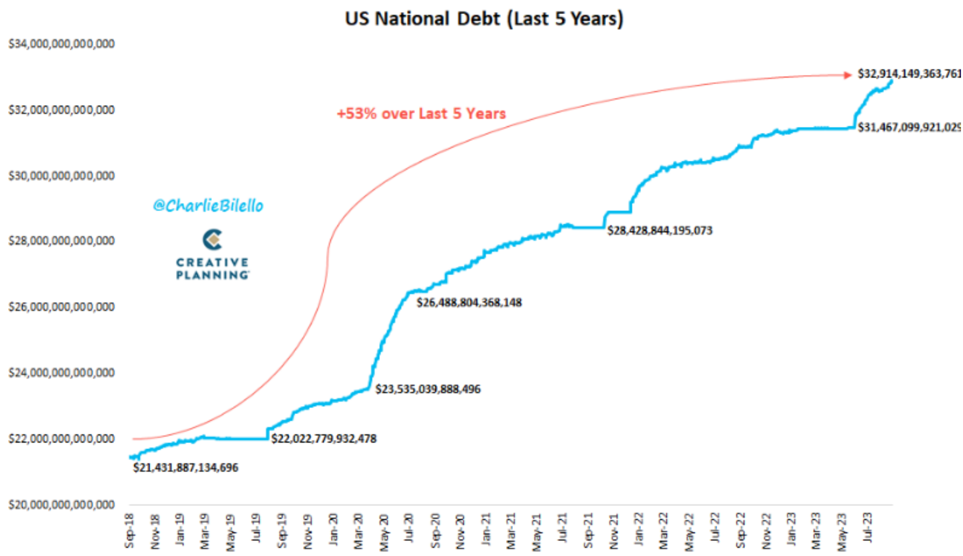
The career politician has also grown in popularity in recent years as the population has become more polarized and each side has glamorized their leaders. Certain Democrats idolize Barack Obama, Nancy Pelosi, and Alexandria Ocasio-Cortez and certain Republicans idolize Donald Trump, Ted Cruz, and Mitch McConnell.

We know one singular thing cannot explain the chart above but believe it is a blend of things that we have mentioned. It is also important to mention that long-serving politicians usually end up retiring with generational wealth that they can pass on. The wealth is grown despite a mediocre salary. The power, insider information, connections, and even book deals or documentaries are more than likely the major drivers in this recent phenomenon.

Trump and Biden forever

No, we are not going to dive into the 2024 Presidential race that we will all be forced to watch next year. This entry is about debt. Debt that both Biden and Trump added. Yes, there was a pandemic, but do you know how much the two most recent Presidents added onto debt in the matter of 60 months?

The two Presidents added $11 trillion to the national debt in 60 months.



The underlying debt pile jumped by 53% in 5 years, and it was Trump and Biden's doing. Even before Covid-19, Trump added on $2 trillion in debt in 2 years. Biden has added on approximately $5 trillion in debt in just over 2.5 years (some tied to Covid-19, most not).

The debt pile would be lower without the pandemic but both parties would more than likely have handled the economy the same way in the initial stages of Covid-19. Our eyes in 2024 are on a candidate who can have some fiscal responsibility and lower this massive number that we all know as the national debt.

Since 2009 the U.S. has added on over $20 trillion in debt. In the previous 14 years (1995-2009) less than $5 trillion was added on to the national debt pile. Both parties have evolved into parties that promise

the world and spend at will to win votes, there is no responsibility, and many individuals believe they are owed these promises even if the country cannot afford them.

We will have to see what happens in 2024. For now, here are the odds for the next President of the United States.

Election Winner	Odds to win 2024 US election	Implied probability
Joe Biden	+150	40%
Donald Trump	+200	33.33%
Vivek Ramaswamy	+900	10%
Gavin Newsom	+1,200	7.69%
Ron DeSantis	+1,600	5.88%
Michelle Obama	+1,600	5.88%
Robert Kennedy Jr.	+1,600	5.88%
Kamala Harris	+3,300	2.94%
Tim Scott	+4,000	2.44%
Glenn Youngkin	+4,000	2.44%
Nikki Haley	+5,000	1.96%

Bank of Canada pause

For all those investors in Canada bracing for the September 6th policy decision by the Bank of Canada, you can breathe a sigh of relief as the Central Bank decided to halt its interest rate hikes. Investors, homeowners with variable-rate mortgages, and prospective home buyers can breathe a sense of relief for now.

The Bank of Canada's overnight lending rate currently sits at 5%. Most economists believed this pause was on the way but beyond this past meeting, experts are quite split on where they think rates will go next.

In a written statement, the Bank of Canada highlighted weakening economic conditions as a reason for pausing its interest rate increases but mentioned that they are prepared to increase policy interest rates further if need be.

The Bank of Canada is scheduled to make two more interest rate decisions this year on October 25th and December 6th.

OPEC+ versus the world

Oil prices have fluctuated over the last 3 years quite substantially. Despite a slowdown in China and recession fears, oil prices are at a 10-month high, prices not seen since last November. As you may remember, oil prices peaked at $120 per barrel last June because Russia invaded Ukraine, a major oil producer that was sanctioned by the West, decreased the global supply of oil sending oil prices sky high. However, in the months (and almost a year) following energy prices decreased quite substantially, (oil reached the low $60s this past spring) recession fears, demand destruction fears, and countries not following their sanctions led oil lower.

This decrease in the price of oil was a major driver in inflation rates slowing down across the world as oil, auto fuel, electricity prices, and other energy fuels decreased in price quite substantially year over year and thus decreased the CPI.

Even with these fears and these narratives, we continued to remain in the camp that the oil market was too tight and oil prices would soon return to new highs. Decades of underinvestment in the industry, overregulation, and a lack of supply still were huge issues in a market that the world relies on (despite what the greenies tell you).

As oil has risen in price in the past few months (reaching the high $80's this week), our thesis has continued to remain intact. The U.S. has bled its strategic petroleum reserves dry (to a 40-year inventory low), U.S. oil, distillates, and petroleum storage reserves are draining every week, and Western countries are over-regulating the fossil fuel industry. This has caused oil prices to move higher. These Western issues have been accelerated by OPEC+ who have decreased their daily production numerous times this year to offset Western interference in the oil market. Saudi Arabia and Russia have quite substantially decreased their oil production this year and have surprisingly stuck to their words. As oil prices go higher, expect the CPI to heat up. It also seems like these countries in OPEC+ are for the first time all on the same page, and not flooding the market. This unity from OPEC+ tied with a lack of Western investment in the oil industry will result in a few things moving forward:

1. Higher oil and gas prices globally
2. A higher CPI in the mid-term
3. More power for OPEC+ members

If you think it's too late to invest in the sector, you would be wrong. We think the cycle is just getting started, and triple-digit oil will be here before you know it. On the equity side, we believe security selection will be key to making money in this cycle. Look for clean balance sheets, positive cash flows, and growing earnings when looking for energy producers. The other thing that we will mention is to look beyond the exploration companies and the full-service oil and gas companies. There are segments of the market that have lower risk and are tremendously undervalued in today's prices.

We will continue to watch the oil industry and adjust our views as we digest data. There are higher risks involved in investing in commodities so make sure to protect yourselves.

Regardless of how you feel it seems Saudi Arabia's global influence is growing day by day and it looks like they could be the new Switzerland. When we say Switzerland, we mean neutral and a country that deals with everybody no matter the side (in today's terms the East and the West).

Perhaps this shift could provide investors with some diversification with less reliance on traditional markets that investors have targeted. For now, the biggest risks remain in China and the U.S. for a variety of reasons. Either way, we think this is a major shifting trend that we will keep an eye on.

MacNicol & Associates Asset Management
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