THE WEEKLY BEACON **November 29, 2024**

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.

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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.

Ortona Lighthouse, Ortona, Italy

The Ortona Lighthouse is a 79 foot lighthouse located in the Adriatic Sea, off the northern coast of Italy. The lighthouse was built in 1937 and still remains active today.

East Brother Island Light, San Pablo Bay, California

This current lighthouse was built in 1969 in the Bay Area of San Francisco. The lighthouse stands at 48 feet tall and the light station was established in 1874.

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

The great American way

U.S. stocks continue to blow the world away. The 15-year bull market that American equities have been on since the financial crisis has been euphoric. What has arguably gone under the radar during this time is the relative outperformance by U.S. stocks over other areas. We are not comparing U.S. stocks to stocks in emerging markets with elevated risks, we are talking about developed markets that are peers of the U.S.

The chart below tracks European stocks relative to U.S. stocks. (when the chart is ascending Euro stocks relatively outperform, when it descends, U.S. stocks outperform).

Before you say "Wow, Euro stocks must be a steal", we would like to share some data. Yes, stocks for the most part trade at more attractive multiples across the pond, however, the overall economy in Europe (especially developed nations) has seen much slower growth than the growth we have seen in the U.S. Economic growth matters and it's a major driver of stock prices. That is why growth is most attractive in emerging markets expected to grow at high values moving forward.

However, we would recommend to our readers to look across the pond for one-off value plays that have growth potential. There are a few names that catch our eye at first glance.

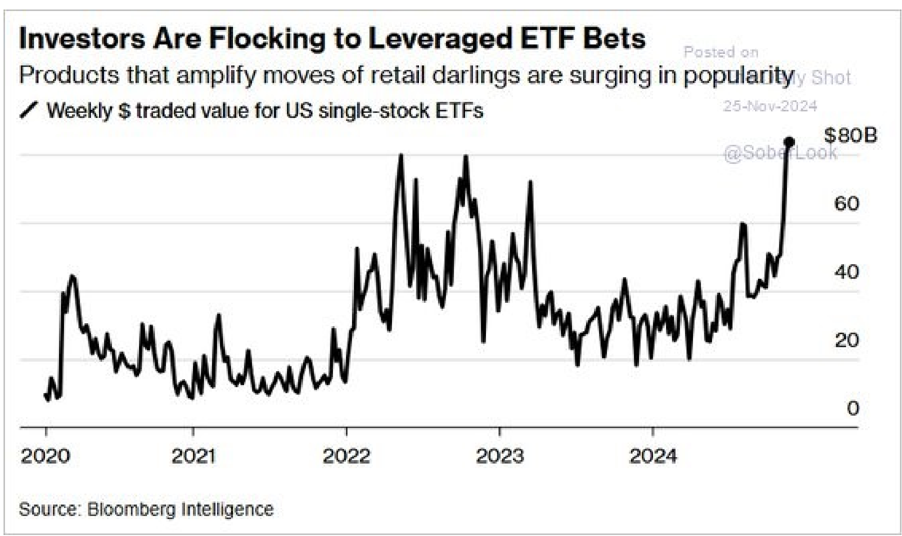
This relative outperformance by U.S. equities has led to U.S. companies accounting for almost 50% of the global equity markets' market capitalization.

If you ignored U.S. stocks in recent decades, chances are you have underperformed.

Not going to end well

Investors more than ever are chasing returns. How do we know this? They are impatient and we follow the flow. Patience is a key attribute most successful investors have, many retail investors do not possess this attribute.

This week Bloomberg reported that investors, specifically retail investors are flocking toward leveraged ETFs at record rates. Leveraged ETFs are securities that use derivatives and debt to amplify the returns of an underlying index or other assets it tracks. Leveraged ETFs have become more and more popular in recent years. There are leveraged ETFs for sectors, sub-industries, and even single securities like Nvidia, Meta, or Tesla. Below is a chart that tracks the weekly inflows in single-stock leveraged ETFs over the last 4 years:



Investors utilizing leveraged ETFs are either extremely confident in an investment thesis or are chasing returns, either way, they want to amplify their returns.

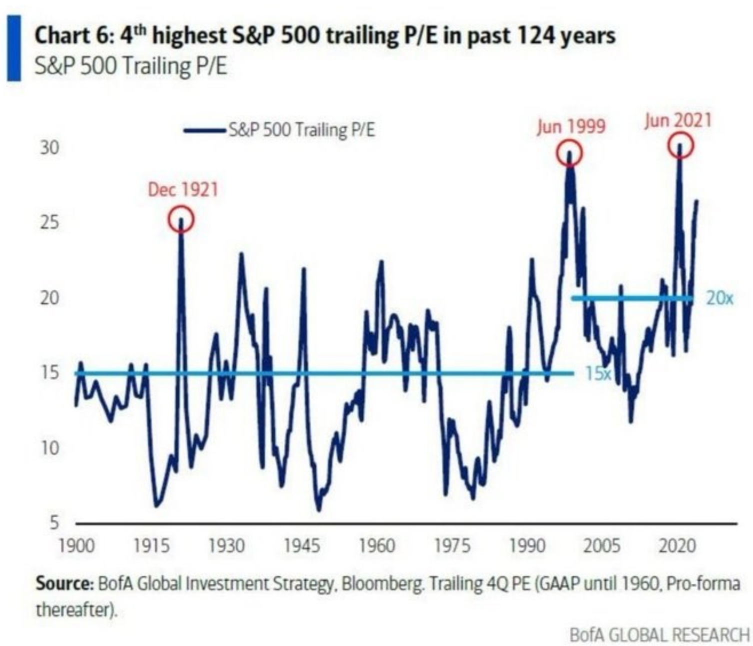
Michael O'Rourke, chief market strategist at JonesTrading said to Bloomberg in a statement that we are in a buy everything phase of the market and there is rampant speculation on par with the 2000 peak. The head of options cited that the popularity of these leveraged products is increasing underlying volatility in certain areas of the market as ETF providers are forced to rebalance daily.

We do not own any leveraged ETFs and would not recommend that our investors and readers buy them. These ETFs have extreme risk and can plunge significantly on any given day. Investor flows like the one we have described above tend not to end well, especially for retail investors.

Despite speculation being at its highest point since the Financial Crisis, many investors continue to pile in. We prefer quality names that can be long-term holds (strong investments), over speculative expensive leveraged companies that lack fundamentals.

<u>Markets are not as expensive as other peaks</u>

Just because some stocks are uber expensive and we would not touch them with a ten-foot pole, it does not mean everything is expensive or that the underlying index is expensive. According to Bank of America Global Investment Strategy, the S&P has not yet reached the peak trailing-twelve-month price-to-earnings ratios seen in past market cycles.



Yes, they are expensive relative to historical averages but according to this chart, we have seen stocks at higher multiples three times over the last 105 years. Despite not being at an all-time high, stocks are still expensive according to this indicator. This is yet another cautionary warning to our readers to look for quality, safety, and diversification in their equity portfolios. Downturns in equity markets often happen when investors least expect them. The run that markets and growth stocks have been on over the last 10-20 years has been historic. Despite this run, retail investors continue to pile into stocks at record rates. Retail investors are also the least concerned about a market crash since 2006.

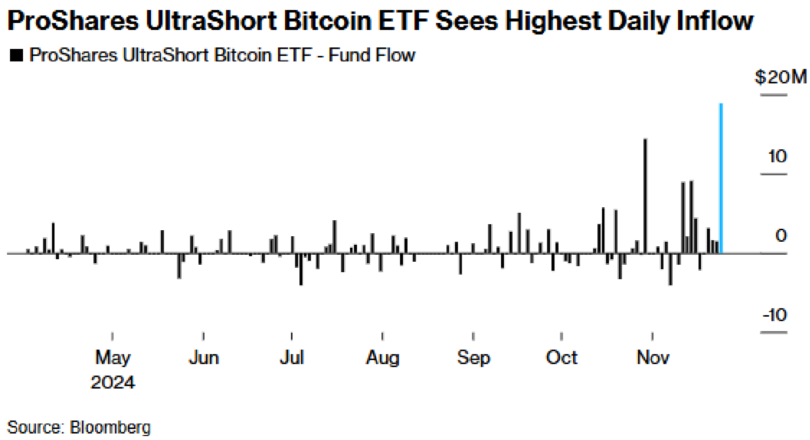
Euphoric runs and improving sentiment have seemingly clouded investors' mindsets. Many investors have limited diversification, and their portfolios are not protected to the downside. We hope you are.

A Bitcoin warning

Bitcoin has gone on quite the run this year. Crypto bulls are on their high horses as markets continue to melt up. Trump winning the election earlier this month was the cherry on top in 2024 for crypto. Trump is expected to slash regulation and will be pro-crypto. However, despite this melt-up, we wanted to share a chart that could point to where the price of Bitcoin could move in the coming weeks to months.

In recent months, Bitcoin's price has correlated heavily with the U.S. M2 Money Supply. However, the money supply is breaking down and is expected to move down sharply. We think this dynamic is one of the reasons Bitcoin's price has recently broken down. When liquidity dries up, speculative assets see outflows quickly. We expect a flight to quality as the trend above continues in the coming months.

Just as liquidity dries up, investors are betting against a price decrease in Bitcoin at record rates. On Monday, the ProShares UltraShort Bitcoin ETF saw $19 million in inflows, a daily record. Investors are seeing what the chart above is telling us.



U.S.: still dependent on Russia

After two years of war in Ukraine, you would think the U.S. and the West would have rotated their dependence away from Russia by now. They have placed sanctions on numerous industries and decreased their reliance on Russian goods and commodities. However, the U.S. remains dependent on Russian uranium. On November 14th, Russia stalled shipments of enriched uranium to certain countries including the U.S. This creates issues for numerous companies around the world that depend on that Russian supply and could pose significant risks for a ramp-up of small modular reactors in the U.S.

The U.S. currently has 94 reactors. These reactors have supplies of enriched uranium stored up. So in the short term, risk is mitigated. However, if this Russian ban is indefinite, prices could be sore. This also puts pressure on U.S. companies and the government to develop a domestic uranium supply chain.

A uranium enrichment company based in Maryland was notified by its uranium supplier in Russia that its import license had been revoked after the Russian ban earlier this month. The stock price of this company dropped by more than 10% over the last month. The American company disclosed that their Russian supplier is looking to find a way to solve the issue with Russian authorities but there is no certainty whether licenses will be reissued.

This news is not surprising as a whole and is something we expected. Earlier this year, the U.S. banned Russian uranium imports but had allowed for waivers of the ban for years as they understood the rector companies had few other options to secure supply.

While uranium itself is somewhat abundant, there are very few enrichment uranium providers across the globe. There are even fewer in the U.S. This puts numerous utility companies at supply risk.

Securing domestic uranium enrichment capacity is a national security issue that should be a major focus for any administration. Securing this supply will be critical for powering data centers as numerous tech companies have announced nuclear deals that will supply them energy moving forward for their AI initiatives powered through their large data centers.

Disclaimer: MacNicol & Associates Asset Management holds various uranium securities including uranium mining companies and the Sprott Physical Uranium Trust across various client accounts.

Brazil goes virtual

A Brazilian Bill was proposed earlier this week that would create a national Bitcoin reserve with a target weighting of up to 5% of international reserves. A Brazilian Federal deputy introduced this legislation which aims to diversify the country's Treasury assets and support the country's central bank digital currency. The assets would be managed by Brazil's Central Bank in partnership with the Ministry of Finance. The organizations would use cold wallets for security.

The proposed legislation also includes provisions for educational programs that would inform the public about digital assets and this new growing financial sub-industry. The legislation states that the implementation would be gradual and buying the assets would come through a controlled acquisition process.

The Bitcoin Sovereign Strategic Reserve would allocate up to $18.6 billion from the country's international reserves. The Bill aims to modernize the technological and finance management in Brazil and make the country more competitive in the digital economy. The legislation specifically points to countries that have successfully integrated blockchain technology into national finance including El Salvador's strategic reserves, the U.S. adopting ETFs, Dubai's efforts to become a crypto hub, and the MiCA regulation in the EU.

The legislation notes how crypto has become mainstream and is a viable asset class. The legislation also noted the asset class's high volatility.

The legislation also states that the Ministry of Finance in Brazil would be required to report on any acquisitions, performance, security, and risks every 6 months. The lawmaker who proposed this legislation stated that a Bitcoin reserve could enhance Brazil's economic resilience to currency fluctuations and economic uncertainties.

Industry experts said this Bill proposal is similar to one proposed in the U.S. Senate by Senator Cynthia Lummis in July. At the time the Bill had limited support. It is unclear how much support this Bill in Brazil would get. Regardless more and more people are waking up to the crypto reality and are looking to hedge against currency risk.

MacNicol & Associates Asset Management
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