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QUARTERLY INVESTMENT OUTLOOK
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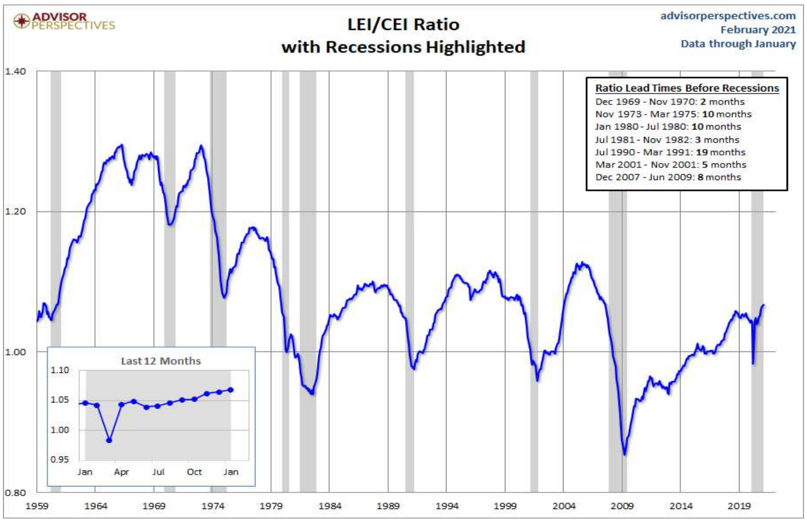
SUMMARY

- The U.S. dollar is in a bear market. This should lead to higher commodity prices and ultimately benefit Global ex-U.S. equities. We expect global to outperform U.S. equities in 2021. The rapid rise in U.S. bond yields could temper the advance in equities, thereby dampening the rise in yields.
- The U.S. growth outlook favors a continuing cyclical recovery as shown by the trend in both the Conference Board's Leading and Coincident Economic Indicators. We follow a ratio of the LEI to the CEI which leads both recessions and recovery phases of the business cycle.
- China's credit impulse at +9.06% suggests that the uptrend in industrial metal prices should continue.
- A monetary regime change is a necessary condition for higher inflation. This happened in the early 1920s and 1970s. In our opinion the U.S. Government's willingness to run twin deficits, which are likely to be funded by the Fed (buying $80 billion of treasuries every month) is a regime change. Higher inflation/bond yields are inevitable.
- Gold prices have been consolidating since August 2020. Gold miners have corrected by 25% and trade at historically low levels relative to the bullion price. We anticipate significantly higher gold prices and are bullish on the miners.

THE U.S. GROWTH OUTLOOK IS FAVORABLE

We find it useful to monitor trends in both the Conference Board's Leading and Coincident Economic Indicators. The chart to follow, courtesy of dshort.com Advisors Perspectives, shows a ratio of the LEI to the CEI. The ratio led all seven recessions (1969-2007) by an average of 10 months with an average lead time of 9.1 months. The current cycle is supported by a prodigious expansion in both monetary and fiscal policies. As a result, both the LEI and CEI are trending higher, although the momentum is slowing. The Conference board expects real GDP to expand at a 2% annual rate in the first quarter. The Federal Reserve Band of Atlanta GDP Nowcast is expecting much stronger 1Q21 growth at over 9%.

The bottom line is we believe the U.S. economy will remain recession free in 2021, which is positive for a continuing cyclical advance in risk asset markets.

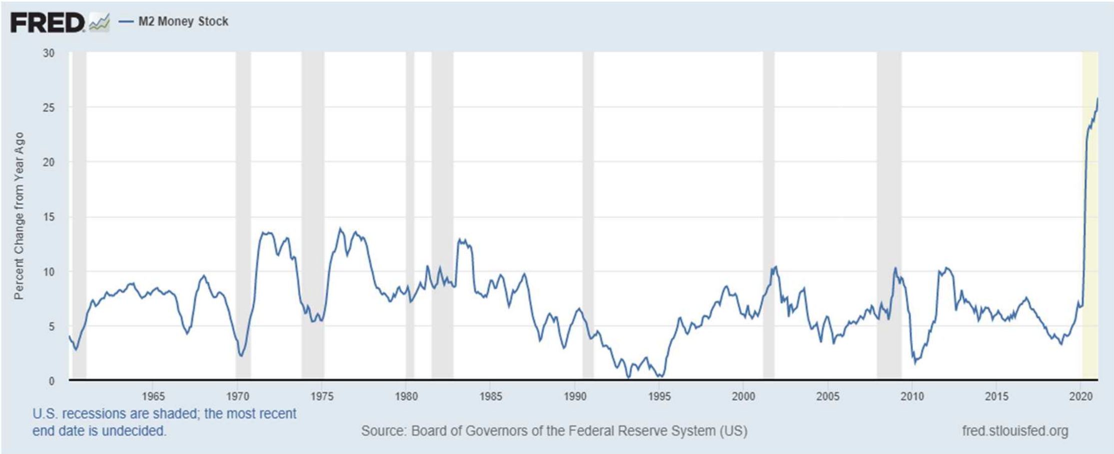


Moreover, we anticipate a global synchronous recovery in 2021 with the U.S., Eurozone, and China all in expanding simultaneously. Both Europe and China are more open economies versus the U.S. As such, they are more dependent on global exports for growth. Global exports have shown a solid recovery but are still negative on a yoy basis. Both the European Central Bank and the People's Bank of China are maintaining accommodative monetary support. Therefore, we expect global export growth to continue improving, a positive sign for forward earnings.

The rapid rise in treasury yields to 1.60% adds a bit of caution to the near-term U.S. growth outlook. Equities are trading at 22x forward twelve months earnings and could be vulnerable to a temporary setback. This could temper the rise in yields, which may serve to extend the cyclical bull market. As the late John Templeton said, "bull markets don't die of old age; they are murdered by the Fed." Fed chairman Powell has made perfectly clear that he has no intention of preemptively acting to remove monetary accommodation by either raising rates of tapering the bank's balance sheet.

A MONETARY REGIME CHANGE IS A PRELUDE TO HIGHER INFLATION

In the early 1920s, following WWI and again in the early 1970s with the Vietnam war ending, there was a monetary regime change. In each case the general price level was inflated. We view todays zero interest rate policy coupled with an unprecedented expansion of the Fed's balance sheet to over $7 trillion as the third monetary regime change in the last one hundred years.

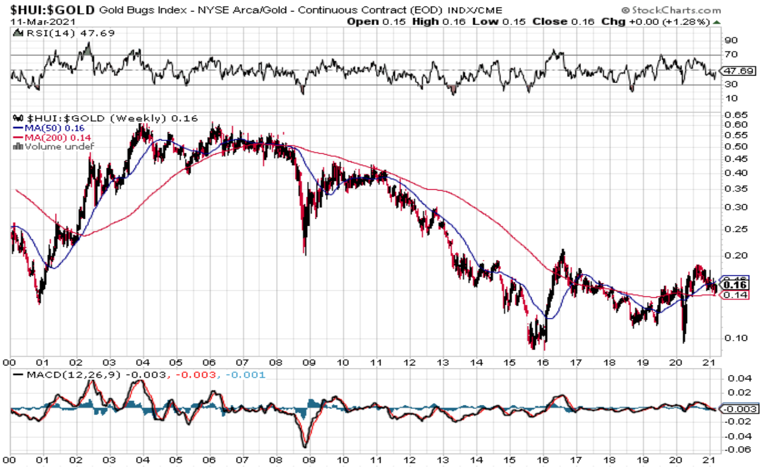


Shown above is a graph depicting the year over year change in M2 money supply. Following a period of relatively subdued money growth over the past ten years, M2 exploded over the past twelve months to a growth rate of 25.7%. This is roughly 2x the money supply growth rate in the 1970s when inflation exceeded 10%. We are unaware of any economists that are forecasting double digit inflation. In fact, few see any significant upward pressure on the general price level over the next few years.

The link between M2 growth and GDP is money velocity. It is defined as GDP ÷ M2. We have shown that money velocity is positively correlated with bond yields. Falling yields leads to declining velocity and rising yields induce higher money turnover. The theory behind this relationship is as follows: declining yields cause savers to increase their demand for savings which, other things being equal, lowers money velocity. As yields rise investors tend to increase their spending which increases velocity.

GOLD PRICES CONSOLIDATING OFFERS BUYING OPPORTUNITY FOR THE MINERS

As noted above a correction in stock prices would likely lead to a cap in the rise in yields. A brief risk off phase in equities could be the catalyst that drives money into gold. We remain bullish on gold if real interest rates are negative. Gold remains an excellent store of value and is owned by virtually all central banks. Over the long run, digital currencies may evolve as a viable investment alternative.

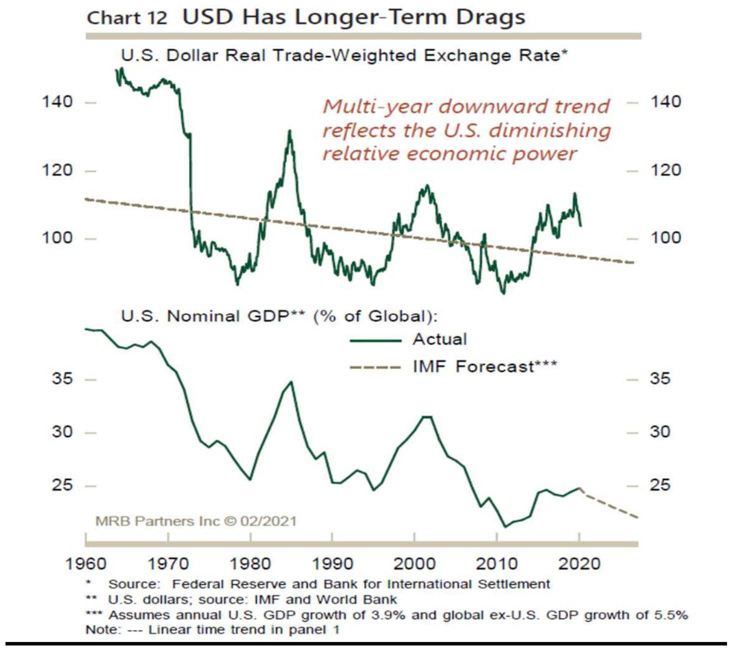


The chart above depicts the ratio of the Gold Bugs Index to the Gold Price beginning in 2000. The ratio has ranged between .60 and .09. Since gold bottomed at 1030 in 2015 the ratio has remained below.20 and is presently at .15. This low ratio suggests that gold miners are undervalued relative to gold. Sprott Asset Management, a noted gold mining research firm, noted in a recent study that on average, miners trade at 7.6x enterprise value to EBITDA versus a 16x multiple for the S&P 500. They noted this is a historically low valuation for the miners relative to the market. We remain bullish on both gold and selected gold miners. Gold should be an excellent hedge against the inexorable decline in the dollar and could gradually replace bonds serving both as a contra cyclical asset class and portfolio risk mitigator.

THE U.S. DOLLAR HAS LONGER-TERM DRAGS

The dollar index is testing a critical multi-year support level at 90. We remain bearish on the dollar. It is being driven lower by two long-term trends. First, is the deteriorating outlook for our twin deficits i.e., fiscal budget and current account. According to a recent study by Double Line taken together they currently approximate an estimated 17% of GDP. This is the largest deficit in history and compares with an estimated twin deficit of 12% in 2010.

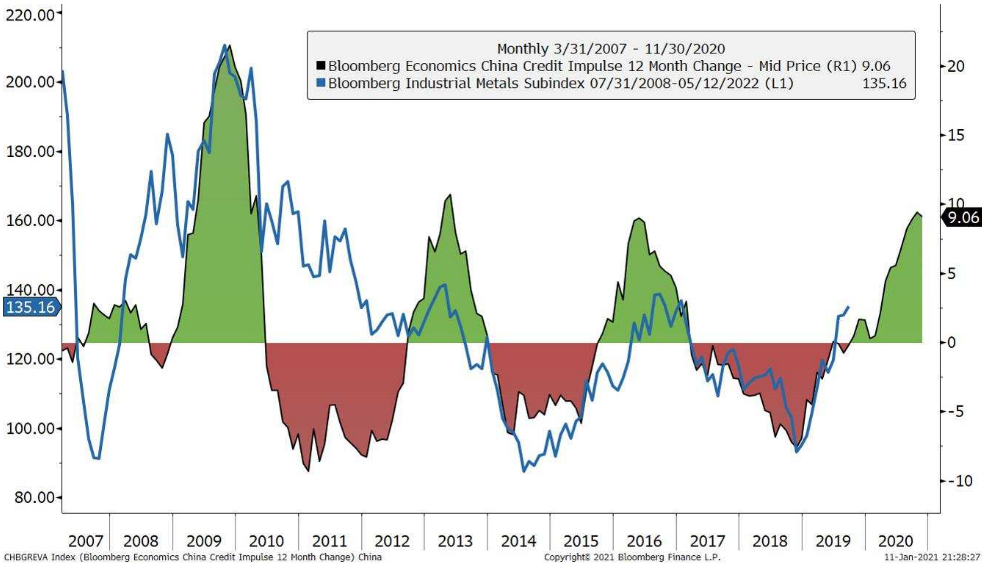
The chart to follow, courtesy of MRB Partners shows the real trade weighted dollar plotted against the U.S. nominal GDP (% of Global GDP). Since 1960 the U.S. has experienced a gradually declining share of world output. The IMF Forecast is expecting this trend to continue over the next 10 years. They project U.S. growth of 3.9% and global ex-U.S. growth of 5.5%. All things being equal this should result in a lower demand for dollars and a weaker exchange rate.



CHINA CREDIT IMPULSE DRIVING DEMAND FOR INDUSTRIAL METALS

In the depths of the pandemic in March 2020, copper briefly traded below $2.00/lb. Presently copper is trading above $4.00/lb. Goldman Sach's commodity head, Jeff Currie, recently stated that he expects copper to be in supply deficit for several years. He cited the growth of renewable energy and electric vehicles as a major demand driver. General Motors recently stated it expects to be 100% electric by 2035. Bill Gates newly released book "How To Avoid A Climate Disaster" claims we need to double our electric grid capacity by 2050 at an estimated cost of $2 trillion.

China accounts for roughly one-half of global copper demand estimated to be 21 million tons per annum. The chart on page 6, courtesy of Double Line, depicts China's credit impulse (aggregate credit as a percentage of GDP) shown in green which was 9.06% as of 01/11/2021. The blue line is the Bloomberg Industrial Metals Subindex which is positively correlated with China's credit impulse. We remain bullish on copper as long as China's monetary policy is accommodative.



RISKS

- Bonds yields surge above 2%
- The dollar decline becomes disorderly
- Global exports falter

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April 2021