

“Let me issue and control a nation's money and I care not who writes the laws.” - Mayer Amschel Rothschild

1

THE FED IS EMBARKING ON ITS THIRD EASING CYCLE OF THE 21ST CENTURY WHILE STOCK INDICES ARE AT ALL-TIME HIGHS, AND THE US DOLLAR IS AT MULTI-YEAR LOWS.

THIS NEW EASY CYCLE, COUPLED WITH PERSISTENT (AND RISING) DEFICIT SPENDING, CAN LEAD TO HIGHER STRUCTURAL INFLATIONARY PRESSURES - DESPITE THE OFFICIAL INFLATION DATA NARRATIVES IN PLAY.

2

SEESAW PRICE ACTION IN THE MAJOR STOCK INDICES IN RECENT MONTHS MAY HAVE MASKED AN OTHERWISE NOTABLE ROTATION TAKING PLACE - UNDER THE HOOD.

3

HOUSEHOLD PARTICIPATION IN EQUITIES HAS RECENTLY ECLIPSED CENTURY-LEVEL HIGHS - JUSTIFYING THE NEED FOR REDUCED EXPECTATIONS FOR STOCK INDEX RETURNS GOING FORWARD - WHEN HISTORICAL ANALOGS ARE APPLIED.

SECTION ONE

RISK MARKETS ARE NEAR ALL-TIMES - AS THE FED INITIATES ITS 3RD EASING CYCLE OF THE 21ST CENTURY.

Since the start of this century, the US Federal Reserve (Fed) embarked on two distinct rate-easing cycles - both of which led to terminal interest rates at essentially zero percent. Will this new cycle be different from the recent past?

We've been making the case that around the time of the dot.com implosion (2000-2002), something quite substantial occurred to the framework of the monetary system - to a greater degree than anything since the official closure of the gold standard in 1971.

Although the roots of such an accommodative disposition can be traced to the days of the “Greenspan Put” post the 1987 stock market crash¹, we'd make the argument that the real show got off the ground when episodes of monetary easing were united with a seemingly unending supply of fiscal accommodation. Since 1997, the US Government has failed to pass a complete fiscal-year budget on time. Instead, federal spending has been based upon an unending series of continuing resolutions. Not coincidentally, spending levels have grown by +285% since Jan of 2000 - dwarfing the increase in total tax revenues (+140%)².

WE CAN GUARANTEE CASH BENEFITS AS FAR OUT AND AT WHATEVER SIZE YOU LIKE, BUT WE CANNOT GUARANTEE THEIR PURCHASING POWER. / ALAN GREENSPAN, CONGRESSIONAL TESTIMONY, 02.16.2005

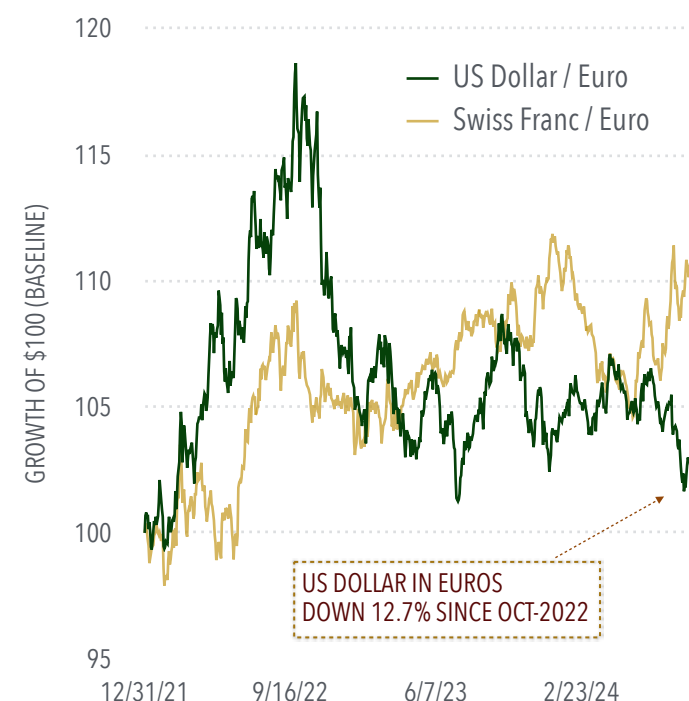
Today, the situation has the makings of a runaway train as deficits have exploded in recent months - even as pandemic-related spending has ended amidst near record Federal Tax Revenues. Hence, we remain focussed on what could be a prospective environment replete with increasing levels of complexity.

Although most price quotations are presented in nominal terms, at the end of the day everything in reality comes via a relative equation. And today, we find few truly appreciating the degree to which the US dollar has its lost purchasing power over the past several decades. As the Fed moves to ease interest rate policy once again, this is an important variable at hand for those interested in procuring “real” returns in the period ahead, we would contend.

1 / Bornstein, Gideon, and Guido Lorenzoni. "Moral Hazard Misconceptions: The Case of the Greenspan Put." International Monetary Fund Economic Review, March 2018, vol. 66, pp. 251-286.
2 / U.S. Bureau of Economic Analysis, "Table 3.2. Federal Government Current Receipts and Expenditures" (accessed Tuesday, September 17, 2024).

CHARTING “SAFE-HAVEN” CURRENCIES US DOLLAR VS. THE SWISS FRANC (AGAINST THE EURO)

DATA SOURCE: STOCKCHARTS.COM / AS OF 09.17.24



The US dollar Index has endured a decline of over 12 percentage points since October of 2022. A notable development within this move is the relative (to Euro) price divergence between the Greenback and the Swiss Franc since this past Spring.

RECENT HISTORY: 1ST RATE CUT IN A CYCLE / St. Louis Federal Reserve

Dates of Signals	Initial Rate	# of Cuts	Terminal Rate
August 1, 2019	2.50	5	0.00
September 18, 2007	5.00	10	0.00
September 29, 1998	5.50	3	4.75
July 6, 1995	6.00	3	5.25
July 13, 1990	8.00	18	3.00



SECTION ONE

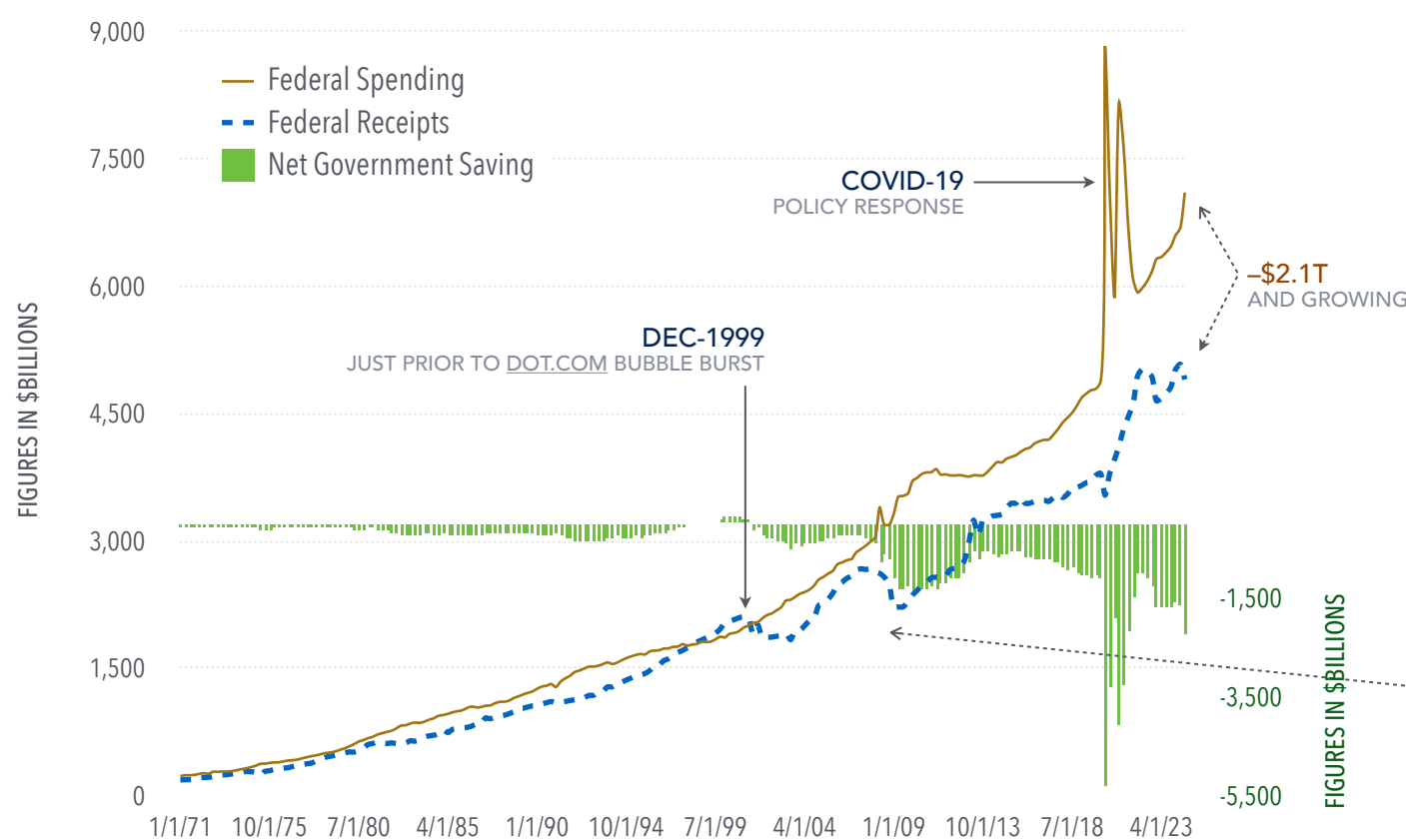
RISK MARKETS ARE NEAR ALL-TIMES - AS THE FED INITIATES ITS 3RD EASING CYCLE OF THE 21ST CENTURY.

As illustrated below, Federal Tax Receipts are essentially flat over the past two years³ - all while Federal Spending is higher by nearly 20%. A vast majority of these increases are attributable to the auto-pilot nature of today's budgeting process - including record social security payments and surging interest payments on the national debt. Using history as guide, we cannot find an analog where the resolution came via widespread austerity measures instituted in advance of a major financial crisis. In fact, every late-stage economic super power (throughout history) chose to inflate such "math problems" away - and we see today's environment containing no special circumstances to delineate from those other occurrences.

Thus, the world of financial instruments in the advanced western economies may require a new lens to help determine the true long-term economic viability of certain investment instruments - especially many of which that have become popularly-employed over the years - arguably through a monocle designed in the 20th century.

FEDERAL SPENDING, FEDERAL RECEIPTS, NET GOVERNMENT SAVING (1971-2024)

SOURCE: BEA.GOV / 09.16.2024



A structural decline in household savings rates (see chart below) can be used as confirming evidence that the multiple series of accommodative actions over the years has created a hidden "tax" on American residents - where they (as a whole) are unable to save even during a period of supposedly full employment and officially manageable inflation. Views from a different lens can help identify the true signals through the noise of potentially faulty price inflation data points. It's quite interesting that the probable solution to what could be termed as an inflationary recession would be to have more economic stimulus (both fiscal and monetary).

NET HOUSEHOLD SAVINGS RATES (1971-2024)

SOURCE: ST. LOUIS FEDERAL RESERVE / 08.23.2024



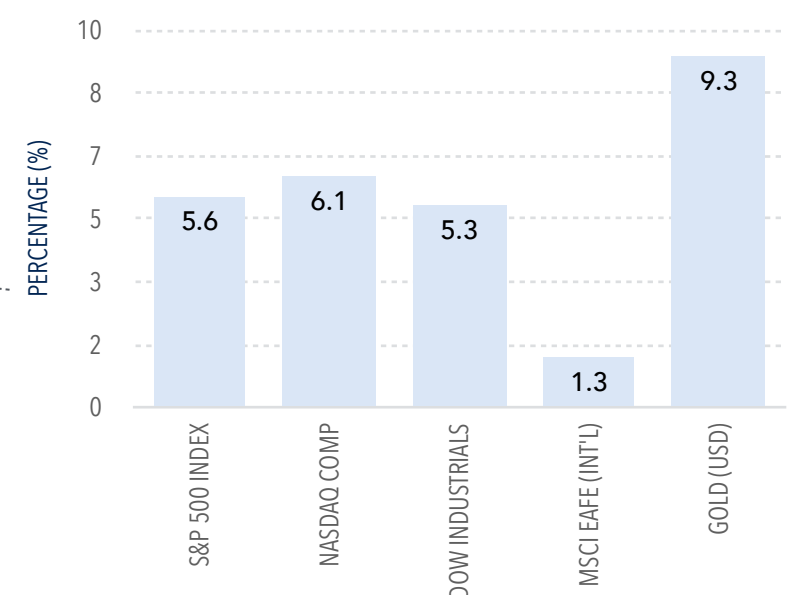
³ / <https://www.bea.gov/data/government/receipts-and-expenditures>

OUR TAKE REGARDING: NEW ROUND OF ACCOMMODATION BY THE FED

Waves of accommodation for the past 25 years (especially) have led to a substantive devaluation in the underlying base currency (US dollar). The degree to which can be illustrated in the chart below. This next series will not likely lead to a different result.

ANNUALIZED PRICE RETURN SINCE 12.31.1999

SOURCE: STOCKCHARTS.COM / AS OF 09.16.2024

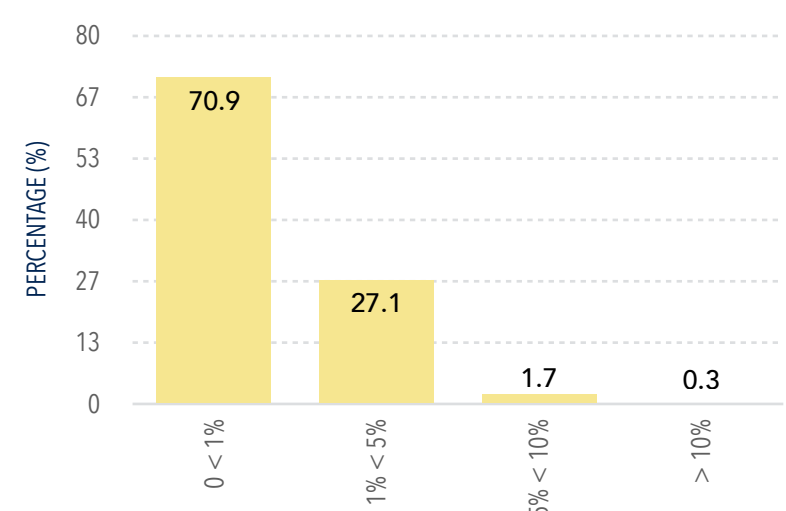


GOLD HAS OUTPERFORMED ALL MAJOR STOCK INDEXES SINCE THE TURN OF THE CENTURY

It shouldn't be a surprise that few investors may know this stat (above) since a vast majority of US investors have supposedly devoted less than 1% of their investable capital towards precious metals (see below). We remain curious as to what set of circumstances may be needed to move this "allocation needle"...

GOLD ALLOCATION BY INVESTMENT ADVISORS (2023)

SOURCE: BofA GLOBAL RESEARCH, CRESCAT CAPITAL, INCREMENTUM AG



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SECTION TWO

AS THE BROAD MARKETS HOVER NEAR HISTORIC HIGHS, THINGS ARE HAPPENING UNDER THE HOOD
MEGA CAP STOCKS HAVE LAGGED SINCE THE JULY-2024 MARKET TOP

With all the talk surrounding the “Mag-7” stocks, we wonder how many have noticed that many of the mega-cap market leaders (dating back the Spring of 2023) have faltered - at least in a relative sense since the start of July. It remains to be seen whether this development will be temporary or more lasting. Given our analysis on the next page, the concept of a probabilistic, risk-adjusted can be factored into the decision-making process.

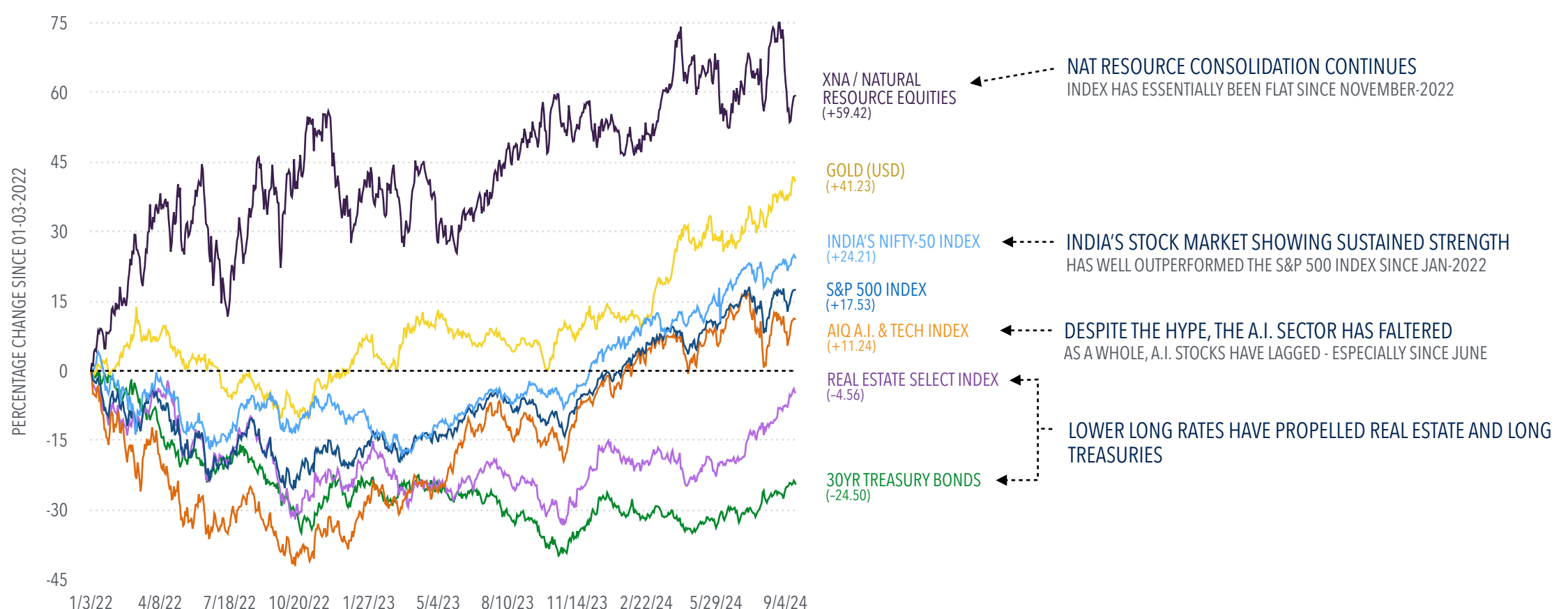
CHARTING THE S&P 500 INDEX WITH THE DUMB MONEY CONFIDENCE SENTIMENT INDEX

SOURCE: STOCKCHARTS.COM / SENTIMENTRADER.COM / AS OF JANUARY 05, 2024



CHARTING PERFORMANCE OF MAJOR ASSET CLASSES SINCE 01-03-2022 (2022 MKT TOP)

SOURCE: STOCKCHARTS.COM / DATA AS OF 09-17-2024





SECTION THREE

THE BROAD EQUITY MARKETS:

THE STAGE IS SET FOR A MAJOR INFLECTION POINT

Investors as a whole historically work to “buy past performance”. The data are irrefutable in this respect - from net fund flows to investor sentiment surveys - there is no more reliable indicator (from a contrarian point of view) than to see how the masses are behaving when working to quantify potential risk versus reward.

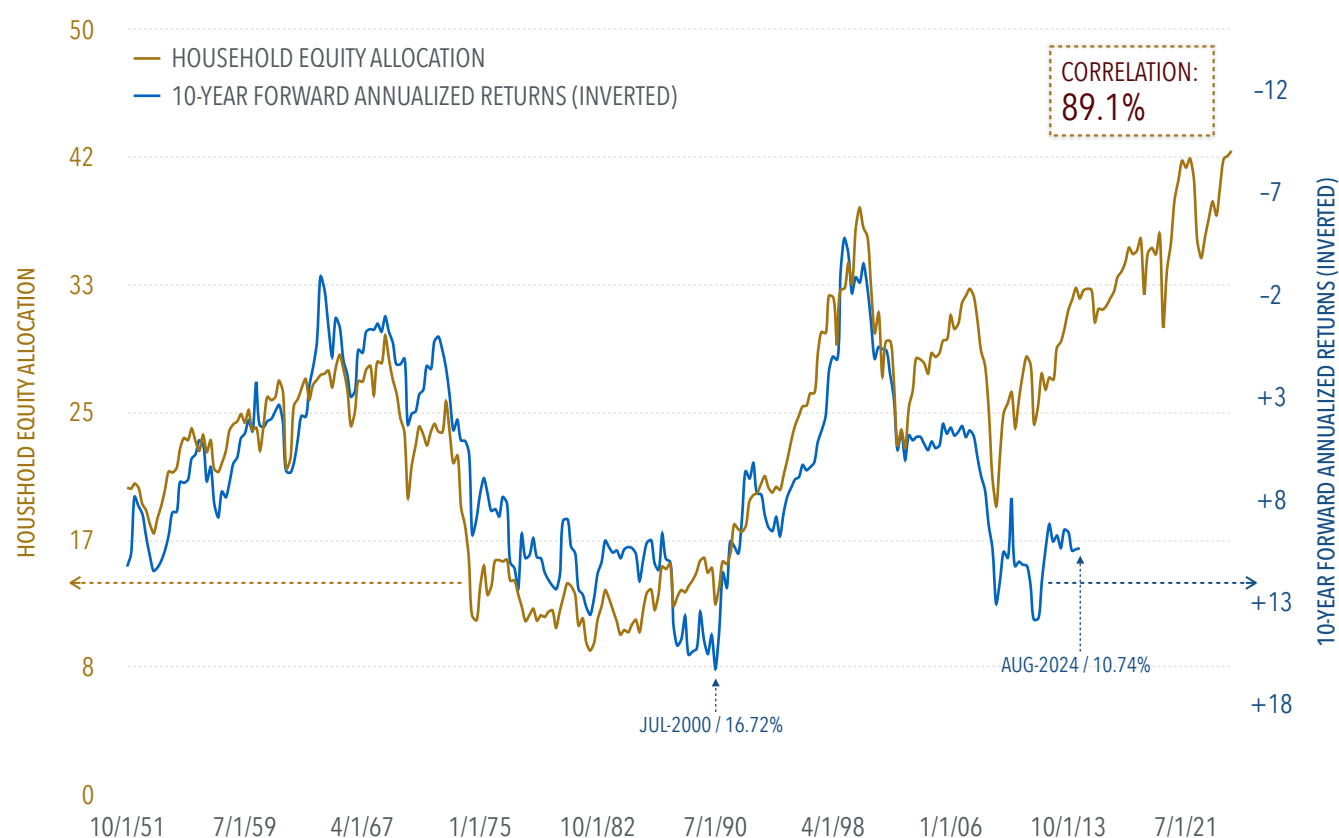
Take, for example, the level of household allocation to equities - now the highest in nearly a century. The correlation between this allocation level and the 10-year forward annualized (inverted) return of the S&P 500 is remarkable. Although this time may be different, especially with the potential of untold money printing to come down the pike, we would contend that this is the time to plan and prepare for the highest probabilistic outcome.

RELATIONAL CHARTING:

HOUSEHOLD ALLOCATION TO EQUITIES (1951-2024)

VS. 10-YEAR FORWARD RETURNS OF THE S&P 500 INDEX (INVERTED)

SOURCE: ST. LOUIS FEDERAL RESERVE, [TRADINGVIEW.COM](https://tradingview.com) / 08.31.2024



HISTORY OF 25%+ DRAWDOWNS IN THE EQUITY MARKETS

TIME TO RECOVERY (NEW ALL-TIME HIGHS) HAS BEEN RELATIVELY SHORT FOR THE PAST TWO CYCLES

“Buy the dip” mentality has been arguably reinforced by the last two substantial drawdowns in the US stock market. The average time for a full recovery (in price terms) for the past two cycles has been 1/5 of the average for the past century - not including the 1929-1954 recovery period post the Great Depression.

25% + Drawdowns since 1928 (Daily Close, Nominal Data)

Date of Cycle Top	Max Draw Down (%)	Time from Top to Bottom (Yrs)	Time to Recover (Yrs)	Average (Yrs)
September 16, 1929	(86.06)	2.78	25.02	4.01
December 12, 1961	(27.59)	0.54	1.72	
November 29, 1968	(30.71)	1.41	1.49	
October 12, 1973	(41.67)	1.15	6.28	
August 25, 1987	(33.52)	0.28	1.92	
March 24, 2000	(45.76)	2.96	7.18	0.81
October 9, 2007	(54.04)	1.42	5.47	
February 19, 2020	(33.92)	0.09	0.50	
January 3, 2022	(25.42)	0.77	1.12	

NOTABLE STATS REGARDING THE ALL-IN MENTALITY FOR CAP-WEIGHTED STOCKS BY THE INVESTING PUBLIC

1. CAP-WEIGHTED STOCKS ARE HISTORICALLY EXPENSIVE
2. A MAJORITY OF INVESTORS NOW INVEST VIA PASSIVE CAP-WEIGHTED INDEX FUNDS, ETFS
3. THESE POPULAR INDEX INSTRUMENTS ARE AT THEIR HIGHEST CONCENTRATION LEVELS SINCE 1929.
4. THE INVESTING PUBLIC HAS INCREASED ALLOCATION TO EQUITIES TO HIGHEST LEVEL SINCE 1929.

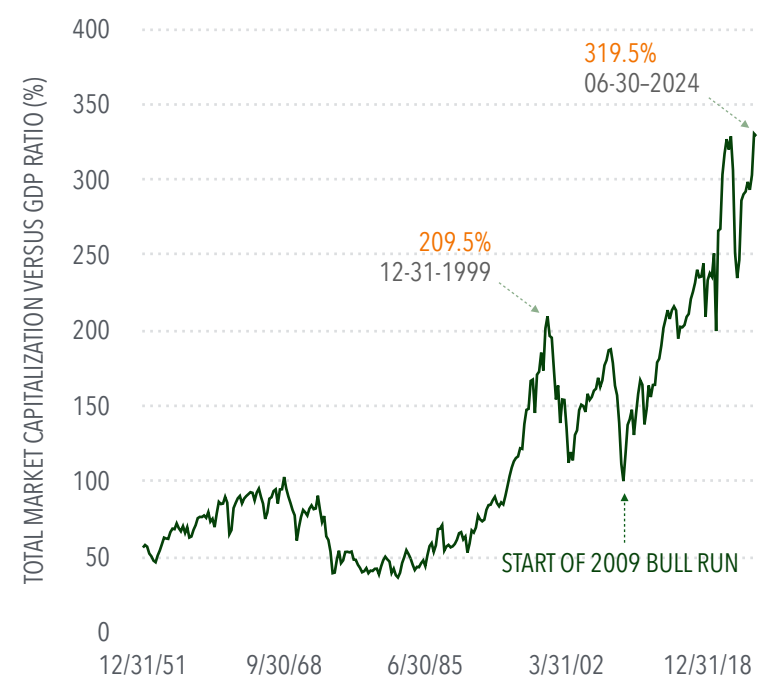
CAP-WEIGHTED EQUITY MARKETS:

MOST EXPENSIVE IN AT LEAST A CENTURY

On the back of a 300% rally in prices for large-cap US equities (which have dominated global equities since 2008), the movement into passive equity instruments is 98% invested into cap-weighted funds and ETFs. Moreover, equity valuations for such instruments are the highest in a century (when comparing overall market capitalization to the size of GDP). Meanwhile, given the true state of the global economy, the probability for future fiscal and monetary accommodation remains elevated at the least. We cannot find an analog to this setup in modern times.

MEASURING THE VALUE OF US PUBLIC AND PRIVATE EQUITIES TO GDP (RATIO)

SOURCE: ST. LOUIS FEDERAL RESERVE (06-30-2024)



UNPARALLELED CONCENTRATION IN HEADLINE INDEXES

TOP 5 HOLDINGS IN S&P 500 INDEX IN % WEIGHTING

STANDARD & POORS / AS OF 09.16.2024





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