Adrian Day
ADRIAN DAY ASSET MANAGEMENT

PORTFOLIO REVIEW

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After years of mostly strong investment markets, spurred on by excessively easy money and ultra-low interest rates, markets around the world and all asset classes have deflated as central banks reverse course and start tightening. The extent of the excesses was such that far more will need to be done to correct them, but even so, we have experienced in the U.S. the most rapid pace of rate hikes certainly since 1980 and arguably ever, resulting in virtually every asset class and market falling. Most of the world's central banks have relentlessly raised interest rates and withdrawn liquidity (some more enthusiastically than others). U.S. stocks, world stocks, bonds both long and short term, crypto, real estate: everything fell in a volatile year, most down by double digits. Gold and silver were unacknowledged champions, by holding their own. Though the rate of tightening might slow, the impact on the economy and markets is by no means over, as we discuss below. The year ahead will be a time to focus on preserving assets while looking opportunistically for mostly short-term trades.

■ Global stocks down across the board

Both U.S. and world equities rallied towards the end of the year—their third major rally during the year––but this was not enough to erase earlier losses. World stocks (per the MSCI World ex-U.S.) were down over 18%, while the S&P closed down over 19% for the year (with the Dow less, Nasdaq more). In Europe, most markets were down in the mid-teens, with the U.K., down a little less than 10%, the best of the major markets. Major Asian markets fell from 15% to almost 30% (China) during the year. Only Singapore and Brazil among major world markets ended the year with positive returns.

In terms of sectors, tech and social media companies were the worst, along with consumer durables, while materials and food were among the best. For balanced portfolios, bonds did not help, with both long and short duration down; the intermediate bond index fell almost 8% for the year.

Global funds (per the Bloomberg Global Equity Index) fell almost 21% for the year. In that context, our global accounts—down between less than 3% and just over 7% depending on risk—were not *so* bad.* (Numbers are preliminary.) Our global accounts rallied strongly in the lasts quarter, up 15.5% for the mid-risk accounts. We outperformed because of our country weighting: with very little in the U.S. (which lagged global markets), the U.K. (top European market) and Singapore (top Asian market) were among our two largest allocations. Our large weighting to gold, silver and some other commodities also helped.

■ Gold holds its own

Commodities, as always, were mixed. Though the Bloomberg Index was up nearly 14% for the year, as many individual components fell as rose. The biggest winners were in the energy complex, with WTI up nearly 7% and natural gas up 20%, while heating oil and other specialty oils were up far more. Coal was up almost 40% and most of the agriculturals were also up for the year. Among the metals, other than nickel (up 45%), most were down.

Gold closed the year essentially flat, while silver was up a little less than 3%. Gold and silver stocks had a strong close to the year, but were still down for the year. Precious metals funds (per the Bloomberg PM Fund Index) were down 7.4% for the year. (Excluding the Vanguard Capital Cycles Fund, which Bloomberg inexplicably continues to include in its "precious metals" index and was the top-performing fund this past year, the gold funds were down over 10% for the year.)

We lagged this year, with our gold accounts down 12.5% (after rallying nearly 16% in the last quarter). The main reason for the under-performance is our large exposure to juniors and exploration stocks, which as a group failed to rally with the market, but held their earlier losses, while a couple of our larger positions had losses as much as 30%. (The SEC, perversely, does not permit us to refer to the performance of individual securities, so we cannot discuss the reasons for the underperformance or our expectations going forward.) In general, we expect the junior names to catch up rapidly in a sustained gold bull market.

■ The main culprit

The main cause of assets of all types around the world collapsing was the tightening policies pursued by the world's central banks, most importantly the Federal Reserve. Other banks raised rates ahead of the Fed and more stringently, but none of the major banks has been as firm. At its last meeting of the year, the Fed hiked rates by "only" 50 basis points (half a point) but emphasized its new message that, though the pace of hikes was slowing, they would remain higher for longer. Fed chairman Jerome Powell said more than once that the conditions were still not "sufficiently restrictive", while Fed members, in their so-called "dot-plot" predicting future economic conditions, raised their expectations for the level of interest rates next year and beyond.

Powell, who little more than a year ago was calling inflation "transitory", admitted that the Fed expected to have made more progress reducing inflation than they had; "it's been more persistent than we thought." The recent dot-plot forecasts are looking for higher inflation over the next several years than in previous such exercises.

■ Enough, already!

However, despite a hawkish message, and a Fed that has in fact raised rates over the past nine months more than many expected, there are signs of a softening. Though Powell was adamant that the Fed would not change its inflation target, as many commentators have cynically suggested, and in answer to a question said somewhat contemptuously, that "we are not even thinking about that", he now says repeatedly that the Fed would "not cut rates until (it is) confident that inflation is coming down towards

2%". That is quite a way from only pausing when inflation is actually at 2% (which itself is a perverse and arbitrary goal for a central bank).

Then there was Powell's parting shot at his important last-of-year press conference: "we are getting close to a sufficiently restrictive rate level". And the Fed would wait for incoming data before deciding whether to hike rates at its next meeting. This was not only extemporaneous answering of questions: the official minutes of the November meeting, just released, shows that "a substantial majority" of policymakers agreed it would "likely soon be appropriate" to slow the pace of interest rate hikes, and Powell repeated this in his press conference.

The emphasis has been on the rate hiking of the Fed, with little said about the other part of the inflation-fighting policy, namely Quantitative Tightening ("QT"), which involves the Fed selling assets on its balance sheet thereby removing liquidity from the system. Indeed, in a rare reference, Powell made a throw-away comment that the Fed is continuing to reduce its balance sheet. This was somewhat disingenuous. In April, the Fed laid out a specific schedule for QT, but it has been consistently behind its own schedule, with the balance sheet coming down from its April peak of $8.965 trillion by approximately $310 billion, rather than the scheduled $522 billion. (Of course, they could have sold the difference in the last week of the year, but I doubt it.)

Powell, again in answer to a question, said that liquidity in the financial system is not a problem, "but if it ever became one, we would cut back on QT." That would not be untoward in such circumstances, but is the first time Powell has indicated that some circumstance might interfere with his apparent single-minded mission to kill inflation. Already the global money supply is down over 8% since its peak in March, while the U.S., falling at a far slower pace, is nonetheless declining at the fastest rate since the Great Depression.

■ Dissension in the ranks

Several Fed officials have recently gone public in calling for a slowing in the pace of tightening, including Rafael Bostic from Atlanta, Loretta Mester from Cleveland, and Mary Daly from San Francisco. And significantly in its annual rotation of voting members, the rate-setting Open Market Committee is losing three supposed "hawks", including James Bullard from the St. Louis Fed, and gaining several doves. Though Powell, as chairman, has the authority to overrule any committee vote (as did Volker several times), a more dovish committee, more focused on the condition of the economy, can certainly add pressure to pause.

Powell is already changing his tune on the possibility of a recession, now saying that "there is a path to a soft, or soft-ish landing". And he appears touchy on the subject, saying he is still looking for positive growth next year and adding, again in answer to a question, "well, if it's positive growth, then it's not a recession." Contrast this with his comments a year ago that just because the U.S. has negative growth doesn't mean it is a recession.

■ How healthy is the labor market?

Powell, and others at the Fed, are placing much of their faith in economic health on the apparent strength of the labor market, continually referring to the strength of the payroll numbers. But there are two labor market reports, the payroll report and the household survey. Without getting into the weeds, these two reports produce their numbers by different means, and there has been a wide and growing difference between the two, with, not surprisingly, the one Powell likes to point to, the payroll report, showing a stronger labor market. The gap is now approaching 3 million workers, so not insignificant, and the statisticians at the Bureau of Labor Statistics must be looking at the reasons for the difference and seeking to reconcile the two.

There is a growing labor shortage that is helping to offset a lower demand, coming from baby boomers retiring; people who stopped working during the pandemic lockdowns not going back to the labor market for various reasons; a lower participation rate; and a rise in people claiming disability. The household survey is more likely to capture people who would like a job but have given up looking. Another factor: in most states, those laid off cannot file for unemployment (whence comes the unemployment rate) until any severance pay has ended, so high-paying employees in Silicon Valley laid off over the summer, will only now be starting to claim for unemployment. For these reasons, we could see a jump in the unemployment number in the New Year and weaker overall labor market reports. This will remove the foundation for the Fed's claims about a strong economy.

■ It will only get worse

A private report, from Challenger, Gray and Christmas, noted that there were almost 53,000 job cuts in the tech sector in November, the highest monthly total in that sector ever. Again, many of these people would receive severance and thus would not be included in the unemployment numbers yet. In addition, businesses, particularly small businesses, are reluctant to lay off workers, doing so only as a last resort. So firms that are struggling now with lower orders will eventually be forced to lay off workers. An added factor in this market is the perceived difficulty of replacing workers, so firms delay laying off underperforming workers. All this reduces the unemployment rate, but also suggests it could get worse as the overall economy softens.

On the other side of the ledger, we are not creating as many new jobs as reported. The BLS estimated net job growth of over 1 million jobs in the second quarter, a number disputed not only by private research firms, but also challenged publicly by the Philadelphia Fed, which said that the estimate was "far too high". It is also worth noting that many new jobs are government jobs with private sector job growth lagging. ADP, for example, said only 127,000 net private sector jobs were created in November, the latest monthly report, well below the estimate, but only just over half the pace of 239,000 seen in October.

In short, the employment picture is not as strong as the headlines, and certainly not as the payroll and unemployment reports, suggest.

■ There is weakness everywhere

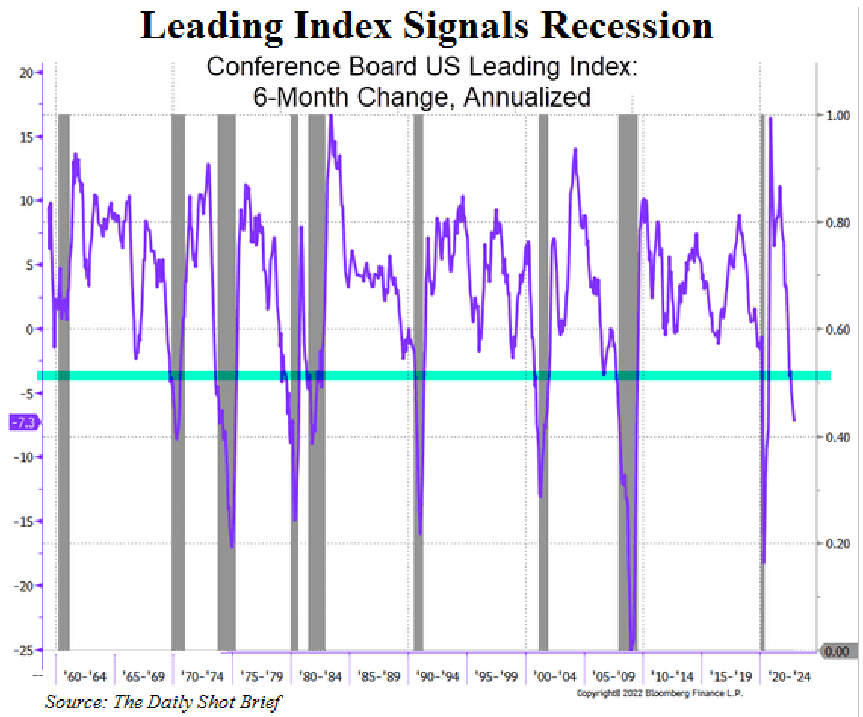
Other sectors of the economy are demonstrating signs of weakness, despite a positive GDP number in Q3. Changes in interest rates have long and variable lags before their impact on the economy is evident. Housing and autos, which are two interest rate sensitive areas of the economy, feel the changes first, but other areas can take a year or more. So we have not yet seen the impact of the tightening already done. (At the end of the 1970s, the Fed Funds rate moved to double-digits in December 1978, and the sustained recession, the deepest since the 1930s, did not start until July 1981.)

Housing has been hit dramatically. Sales have slowed significantly leading to an inventory build up, while pending sales have fallen further than they did in the first two years following the bursting of the housing bubble in 2006. With mortgage rates at virtually 8%, housing affordability has collapsed. People tend to stay put and hold on to a low mortgage rather than move and have to take out a higher-cost mortgage. With fewer pending sales and less traffic, as well as plentiful inventory, prices will soon be coming down dramatically.

There are other worrying signs including high debt levels at both the business and household sectors. Total business debt as a percent of GDP is at 77%, a record high other than the initial covid spike. The personal savings rate has collapsed to just 2.3%; since 1960, it has been lower only for a brief period in July 2005. At the same time, credit card debt has been surging. Spending from savings and debt can only continue so long, so we expect to see lower consumer spending in the new year.

■ Indicators strongly suggest a recession ahead

We could continue looking at sector after sector and signs of current weakness abound. Looking ahead, however, things get more certain. There are two reliable indicators of future recession. First, the inversion of the yield curve, where longer-term rates are lower than shorter-term ones—different economists emphasize the one-year over three-year, or the two-year/10-year spread—but recessions usually follow when the yield is inverted across the curve. Again, however, there is a lag. In fact, most recessions do not start until after the Fed has ended raising rates.



Another powerful indicator is the Conference Board Leading Economic Index, which has declined most months since February and is down about 4% on the year. A recession has always followed such a decline in the LEI. The last decline of this magnitude was in December 2007. To compound matters, the Fed usually starts to cut rates with a negative LEI, but this Fed is continuing to increase rates even as the LEI is dropping.

In previous periods of LEI declines, inflation has been under control, but it is not now. Though the December CPI report, coming in a little lower than expected, was heralded as the beginning of the end, it was still up over 7% year-on-year; it was just 1.3% two years ago. The Producer Price Index remains higher, up 9% over the past 12 months, and producer prices tend to lead consumer prices. The lower oil price—which fell from over $90/bbl to under $75 during November—was the main factor leading to a lower CPI report, but the oil price has been moving back up in December, suggesting, all other things being equal, a higher CPI report for December and January. It is when the economy moves into a recession that we can expect to see the CPI numbers come down consistently.

It seems very clear that beneath the headline numbers, this economy is in trouble, with reliable indicators of future recession clearly pointing in that direction. We suspect that by the middle of this coming year, it will be clear that the economy is in a recession.

■ Global central banks are tightening too, as China re-opens

Other major central banks may be late to the party, but have been trying to catch up with the Fed. Even the Bank of Japan, which has been suppressing yields for years, just last week indicated that its policy is finally changing, as it widened the target range for yields. Not surprising, yields in the market went sharply higher, with the 10-year yield doubling overnight (albeit only from 0.24% to 0.47%). The BoJ move is important in policy terms and will have an impact on markets around the world. It will be negative for global bond markets, positive for the yen and therefore negative for the dollar, and potentially positive for the long-moribund Japanese stock market.

Other significant developments also came from the East, with China backing away from its zero-covid policy and opening the economy. This is positive for regional markets and currencies, as well as for commodities as one can expect Chinese imports to recover. There are clearly certain sectors, such as travel, that should be prime beneficiaries. Contrary to other central banks, the Peoples Bank of China has said that there will be increased government spending to "provide more forceful support for the economy" and expand domestic demand. That may lead to an overheating later in the year.

European Central Bank President Christine Lagarde, who championed negative interest rates little more than a year ago, is trying to catch up with the Fed, issuing a Christmas message that rates will move higher to fight inflation. This comes as the Eurozone is sliding into recession amid high energy prices, but true to form, Lagarde says "the recession we feared will be short-lived and shallow." We'll see how *that* ECB forecast works out.

Germany and the U.K. may already be in recession, while the eurozone will be shortly if it is not already. High energy costs and weak manufacturing and productivity, as well as high debt levels in many countries, will make it other than "short-lived and shallow".

■ Globalization ends with two blocks

More fundamental developments are coming as the world breaks into two blocks, the U.S.-led major western countries, and the rest. China leads a group to find alternative funding mechanisms that avoid the U.S. dollar and Western correspondent banks. This is a long-simmering move to avoid the risk of U.S. sanctions on unapproved activities which received a sharp prod earlier this year with the seizing of some Russian bank reserves. President Putin has said the BRIC countries (Brazil, Russian, India and China as well as some others) are working on "the creation of an international reserve currency based on a basket of currencies." China has already introduced what it calls the m-CBDC Bridge Project which includes Hong Kong, Thailand and the United Arab Emirates for foreign exchange transactions, and is likely to be expanded soon to include other countries, including Saudi Arabia.

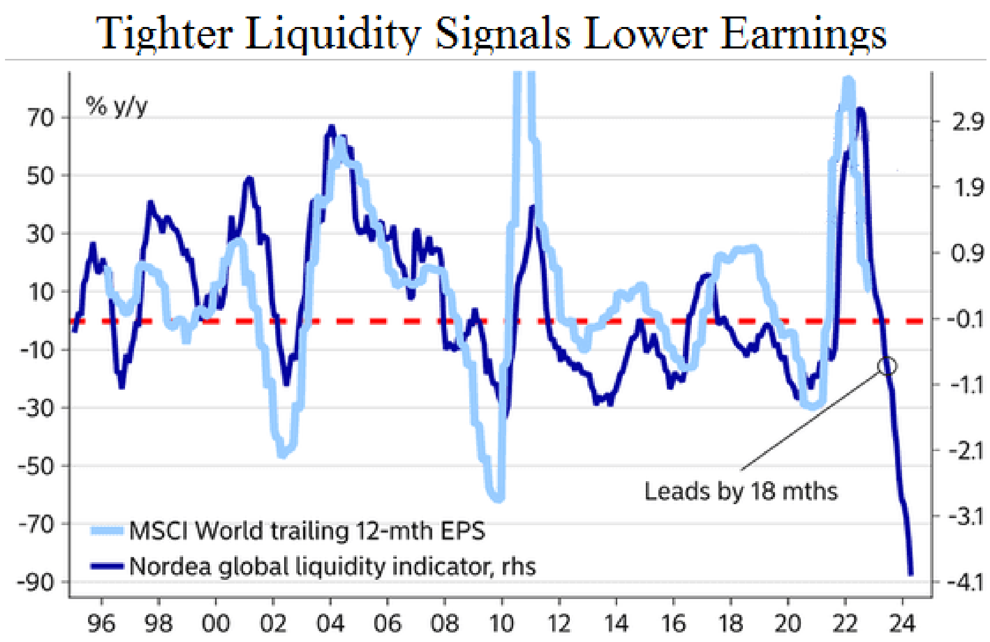
These moves, prompted by the U.S. overplaying its hand one too many times, will have fundamental long-term effects on the U.S. Treasury market, on the dollar (both negative), and on gold (positive) as an alternate central bank reserve asset (see below).

■ Stock markets likely to be weak again in 2023

There have been three significant rallies in the U.S. and other major equity markets over the past year, but each one has failed at a lower level, and declined further than the previous one. Though there is some optimism in certain quarters that the bear market is over, with inflation apparently peaking and the Fed close to pivoting, such thoughts are misguided. The truth is that bear markets take time to play out, as more and more bulls give up. Were the bear market already over, it would have been only half as deep and half as long as most previous bear markets.

It is important to emphasize that even if the narrative of peak inflation and a Fed pause were true, that does not mean that stocks will then bottom and a new bull market begin. No doubt, a clear pause or pivot would see a rally, but not necessarily a new bull market. If we look at previous occasions when rates stopped going up, half of them saw losses of more than 20% *after* the final hike, and of recent occasions, two of three saw losses of nearly 50%. In most historical occasions, the market declined more *after* rates stopped going up than before. This does not mean there will not be rallies; indeed, bear markets have seen some of the largest daily and weekly gains in markets ever. But these are against a background of eroding prices and we must avoid the call of the siren.

We expect corporate profits to decline as built-up inventories need to be disposed of at lower prices—we have already been seeing this over the past month or more—and this will cut into margins and, even if price-earnings multiples are maintained, will lead to lower stock prices. More likely, of course, as earnings fall, there will be multiple contraction as well.



Source: The Daily Shot Brief

On balance, we must expect further declines in the coming year, while value will continue to hold up better than growth, overseas markets better than the U.S., and emerging markets better than developed. In the latest weekly numbers, U.S. value funds have record inflows of $14 billion; global funds had inflows of $18 billion, while most large U.S. funds saw outflows. Our strategy, however, will be to look opportunistically for investment and trading opportunities, including selling puts on depressed stocks, and buying to take advantage of global developments, such as China re-opening or Japan's policy change. In most cases, however, these are more likely to be short-term trades than long-term investments.

■ Resources set to shine

Commodities in aggregate, as mentioned above, had a good year, but returns of individual commodities were mixed and volatile. More investors are beginning to realize that this is a good place to hold funds, with both stocks and bonds vulnerable. As a reflection of that, commodities hedge funds saw a 50% jump in assets this past year.

Generally, we are emphasizing resources driven by shortage of supply rather than expected increases in demand. Certainly, China re-opening will boost demand for resources. But we want resources that can do well even if demand simply normalizes. Right now, this means copper and oil and gas, with uranium as a trade for now.

■ Oil market tight, as OPEC cuts while the U.S. contracts

The oil market is tight, with demand exceeding new supply. Were it not for the release of oil reserves from the Strategic Petroleum Reserve and OECD inventories and lockdowns in China all year, oil prices would have traded higher this year. The recent releases from the SPR were beyond the intended scope of a strategic reserve and brought reserves down to levels last seen in the 1980s. Now with China re-opening and the SPR needing to be replenished, we expect oil prices to continue to move back up.

OPEC is unable or unwilling to increase production; indeed it recently cut output by 2 mbpd, while Russia has seen a loss of perhaps 0.5 mbpd which will only increase if the war continues and the country finds itself unable to procure Western technology to maintain facilities. U.S. inventories are down to the lowest level since early 2004, recently declining by over 2 mbpd as production slows. The politically motivated assault on the fossil fuels industry suggests that this is unlikely to change any time soon as the industry decides against long-term, capital intensive projects. We expect a decline in production this coming year, particularly from shale, because of the rapid decline in reserves and rising costs, as well as disinclination to invest capital in the face of official hostility.

■ China makes its move

A very significant development in the oil industry occurred earlier this month, and it is related to the developments we discussed above about an alternate global payments system. China's President Xi flew to Saudi Arabia and met with Saudi and Gulf leaders. This visit marks the birth of the petro-yuan, the beginning of the decline in the petro-dollar, and a giant step forward in China's control over global resources.

Xi said that China would continue to import "large quantities of crude oil on a long-term basis" from the region, and wants to use its currency to pay for all of it within three to five years. This ties in with the Bridge Project discussed above.

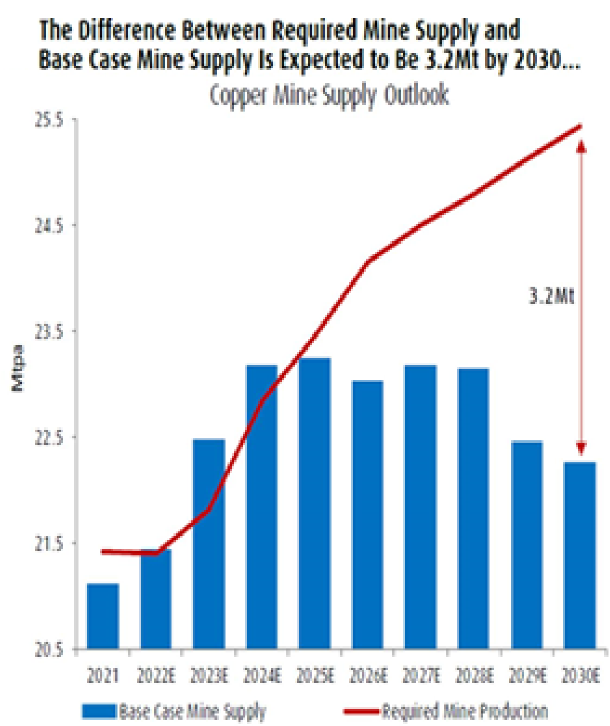
Already, Russia, Iran and Venezuela, which account for about 40 percent of the world's proven oil reserves, are selling oil to China for renminbi at a steep discount. With Saudi and the Gulf states added to that, China is effectively controlling more of the world's oil, and potentially strangling U.S. access, as its own industry contracts.

It was not a coincidence that just as President Xi's plane was landing in Riyadh, the People's Bank of China announced, what the market already suspected, that during the year, it had started buying gold again aggressively.

■ Copper supply growth is constrained

The copper price surged on expectations ahead of China re-opening. We expect increased demand this coming year, but the more important side of the equation is the stagnant supply after years of underinvestment. Project development, other than some brownfields, remains muted, and political problems in Chile and Peru, the two largest copper producing countries, have slowed investment in projects in those countries.

Copper Supply Gap to Widen



Source: Wood Mackenzie, CRU, BMO Capital Markets

Although on paper there could be nearly 10% growth in supply in the next year, there is potential for supply disruptions caused by myriad factors including strikes in Chile, and Russian difficulties in obtaining replacement parts and maintenance. After the next couple of years, however, supply growth is expected to slow to little more than holding its own. This will not be sufficient to meet anticipated base-case demand, meaning higher prices in the second half of the decade.

■ Gold is turning, as investors look for safety

Like Rodney Dangerfield, gold got no respect in 2022, but it ended the year more-or-less flat (down less than 0.3%), an impressive performance in the face of higher interest rates (Fed Funds rate from 0.25% to 4.5%) and a stronger dollar (up 7.6%), two powerful headwinds for gold. This is particularly impressive in the context of other assets and markets that collapsed during the year.

Two things helped gold: amid U.S. weaponizing the SWIFT system (the current global banking payments system which the U.S. controls), central banks looked to move their reserves to assets outside of possible U.S. control; and later in the year, larger investors looked to an asset that would protect them from financial instability and a declining equity market (and crypto wasn't doing the job).

As we wrote in our *Market Insight* sent just before Christmas, investors misunderstood in thinking that inflation alone would boost gold. As we wrote, gold would move when more investors began to realize that the Fed and other central banks would not be able to defeat inflation without causing a serious recession. We discussed earlier in this *Review* that a recession looks increasingly likely; and we have discussed that the Fed is likely to slow the pace of rate increases dramatically next year. Investors are beginning to lose confidence in the Fed's narrative.

If the economy goes into a recession before inflation is tamed, gold will respond; and the dollar will drop if investors think the Fed will pause even as other central banks are ramping up their inflation-fighting rate hikes.

■ Global banks want asset they can control

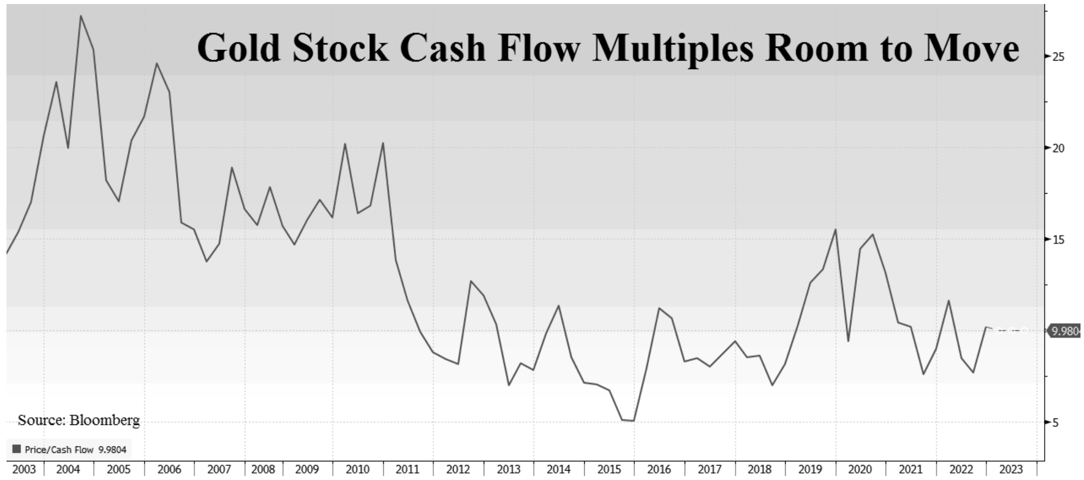
Central banks have been buying gold at a pace not seen since 1967, when the dollar was still linked to gold, with banks buying in the third quarter (year-end numbers are not in yet) more than twice as much as almost any quarter, and three times as much as most, since the financial crisis of 2008. Buyers included Turkey, Qatar, Uzbekistan, India, China and perhaps also Russia. This reflects a move to pre-empt U.S. sanctions and control of the global payments system.

Ongoing central bank purchases, and a slow return by investors, suggest a strong gold market in the year ahead.

■ Gold stocks remain undervalued amidst positive outlook

The gold miners anticipated bullion's $200 jump in the last two months of the year, appreciating 32% since the end-September low. As we discussed in the *Market Insight,* despite this move, the gold stocks are selling well below their historical valuations, while of course cash flows and asset values increase with the price of gold. Senior stocks are trading for less than 10 times cash flow, at the lower end of the historical range; the stocks were over 15x in each year from 2001 to 2011, the last long gold bull market, while they have traded at more than 20x in strong markets.

This recent move well demonstrates the leverage that gold stocks have to bullion, with the stocks moving almost three times as much as bullion. But, as we discussed, the stocks still have a lot of catching up to do to return to their historical ratio to bullion.



Not only are the gold mining stocks undervalued, but the companies are profitable with healthy margins, strong free cash flow, and solid balance sheets, which enable them to pay good dividends (higher, unusually, than the broad market). There are few other assets that are currently in such a strong position, with such a powerful outlook, and yet are so inexpensive.

■ Silver outperforms gold with fewer quality choices

Silver was, as always, more volatile than gold, falling further in the middle of the year. But since the turn in September, silver has moved up two-and-a-half times as much as gold. This is typically a bullish sign for the precious metals. As we have discussed previously, most silver production is by-product from zinc or lead mines; the number of new mines with significant silver production is at its lowest in 20 years. This makes it difficult to estimate silver production in the years ahead, but we expect it to decline even as its demand for both specialized industrial uses as well as investment demand grow.

There are fewer silver producers than there are gold, and even many miners with “silver” in the name or viewed as silver miners actually produce far more gold than silver. This means however that when investors return to the sector, more money will be chasing fewer names.

Overall, we are cautious on global markets, but increasingly positive on gold and silver, as well as some of the other resources. We will maintain our exposure to high-dividend payers in the U.S., as well as to a small handful of global blue chips that are resistant to economic declines. We will be slowly accumulating quality companies in smaller global markets, and looking for short-term opportunities in markets, sectors or individual stocks that have become too cheap or have specific near-term triggers. We do expect to continue to increase cash balances particularly in more conservative global accounts, as we look for, and patiently await, opportunities.

Review of Individual Accounts

■ Global Accounts

Allocations in our global accounts remained more-or-less where they were at the beginning of the quarter, but that disguises more activity than in recent quarters. Exposure to major global markets fell slightly as we reduced holdings, mostly in the U.K., while the allocation to U.S. income stocks

(Business Development Companies and others) remained stable (around 10% for mid-risk accounts and 18% for more conservative accounts). Cash (and cash equivalents such as Treasury bills) increased a little for mid-risk accounts to 6%, and remained stable at 12% for more conservative accounts.

During the quarter, we exited one U.S. stock, a tobacco company, on a rally, and we reduced our exposure to U.K. stocks as they moved up as the political situation stabilized. We are concerned about a recession in that country, so selectively selling the most vulnerable. We also sold some of our BDCs on rallies, while adding to others on declines, ending with about the same allocation.

Three new disparate buys

We have been buying three new stocks: a U.S. investment company run by one of the smartest deal-makers around, cheap on a cash-flow basis and sporting a high dividend; a Brazilian airline, knocked down with the market on the election results, but a beneficiary of the country opening after covid; and a resource-focused mutual fund company, selling below book and at a low-single digit p/e multiple.

We have also bought puts on the S&P, a hedge on accounts against a broad market decline. And we have also been putting spare cash in T-bills and notes, given they now actually yield something!

Looking ahead, we expect to continue to hold our U.S. income stocks, while trading them at the margin; we expect to continue to reduce exposure to major global markets, including the U.K. while building positions in smaller markets, and looking for short-term opportunities around the world; and we expect to continue to hold a high allocation to gold (and trade it at the margin), while building up exposure to select other resources. Overall, we expect our cash levels to remain about the same, fluctuating as we find opportunities or sell others.

■ Gold Accounts

Cash levels increased a little in gold accounts, as we have yet to reinvest all the proceeds from one widely held sale (and some clients have added funds at year end). Cash is now at 2.2% and we expect to return to fully invested in the next few weeks. Otherwise, our allocations remain more-or-less where we started the quarter, a little less than 30% each to seniors and exploration companies, with the rest in intermediate companies and silver and other resources.

Two new development companies with successful managements

We have two new holdings: a company looking to reinvigorate one of the historic mining districts in the U.S., with a top mining executive as executive chair; and a development company in western Canada with a team that has been successful before. We are building positions in these companies.

Yet another of our holdings is the subject of a takeover (not on the most attractive terms, frankly), and we are selling for many clients while holding the new company for larger accounts. In most cases, we are waiting until the new year to sell, to postpone the tax for clients.

Whereas for the last several quarters, most of our buying has been adding to the senior stocks, which are not only the first to move but the most certain to move as the sector turns, in the past quarter we put as much into adding to some of our favorite exploration stocks that had seen tax-loss selling and were particularly inexpensive. This group typically moves later in the cycle, so we remain very selective; the bulk of new money will continue to go to the seniors and intermediates for now.

Looking ahead, we will be fairly quick to reinvest funds and move to a fully invested position again, with a focus on larger companies. As the bull market develops, we will likely look to raise some cash for new opportunities, but the time for this is not yet.

■ Resource Accounts

Cash in resource accounts moved up to 3.3% as, late in the quarter, we received the proceeds from the asset sale we discussed in the last *Review*, and have yet to reinvest it all. As before, gold remains our largest allocation, at about 34% of accounts. Remember, that many gold companies have exposure to other resources, particularly copper, and even oil and gas.

Silver and copper remain our next two largest exposures. In the latest quarter, we have bought two ETFs with exposure to uranium and natural gas. We have owned both before. We tend to trade these because of the structure of the vehicles.

Other than the company whose assets were sold, referred to above, we have sold little this last quarter, reducing exposure to one of the carbon companies which has been disappointing. We have added to top copper companies, before the recent rally.

Looking ahead, we expect to get back to a fully invested position very soon. We intend to hold our gold and silver exposure, trimming as the sector moves up. We will add to copper, oil & gas, and uranium in particular as we diversify the resource accounts; all of these will benefit from China's re-opening.

In sum, we remain cautious about the global economy and major markets. We do not think the Federal Reserve and other major central banks can control inflation without provoking recessions and that will be negative for equities though positive for gold. We are holding our gold positions, building positions in other resources, holding global blue chips, and otherwise looking opportunistically for shorter-term investments. We anticipate our cash holdings will increase in more conservative accounts, but remain fully invested in gold and resource accounts.

Adrian Day. December 31st, 2022