Adrian Day
ADRIAN DAY ASSET MANAGEMENT

PORTFOLIO REVIEW

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The changes in the global monetary system, both from the center and from the periphery, will have as deep an impact on the global economy and the markets as the last major change, in 1971, when the U.S. closed the gold window, ending the last vestige of the gold system. These impacts are likely to be similar to those that followed then: higher inflation, a weaker dollar, and a stagflationary environment, with oil, gold and other commodities performing well, along with emerging market stocks and bonds, while developed stock and bond markets will mostly languished. We are already seeing some of these effects play out.

■ Everything up in the quarter

The quarter just ending saw mostly strong results in almost every asset class and market. Stock markets continued their moves, mostly accelerating the performance of the first half. While the S&P was up almost 8% on the quarter (14% for the year to date), the world ex-the U.S. (per the MSCI All Country ex US Index) was up just under 6% (23% for the year to date). However, most of the major markets had returns in the high single digits, a little more for Asian markets, with the sole exception of Germany, whose market fell marginally (though it remains up a very solid 36% in dollar terms for the year).

Our global accounts well outperformed the benchmarks, with our mid-risk global accounts up 29% on the quarter (and 75% for the year to date). The numbers are preliminary.* More conservative accounts had solid returns, if little less (22% for the quarter and 53% for the year). The main reason for this wide outperformance is our high weighting to gold stocks, that beat every global market.

■ Gold and silver lead the resources

The commodity complex, as always, had disparate returns. The Bloomberg Commodity Index rose just under 3% for the quarter, just over 6% for the year so far, but within that the metals all rose, with gold (up 16%) and silver (up 29%) in the quarter the clear leaders. The energy complex fell, while agriculturals were mixed (with coffee jumping 22%, while others fell).

The gold and silver stocks exhibited some of the leverage we are used to, with the XAU index up 44% in the quarter and 117% for the year.

Our resource accounts had strong returns, 37% for the quarter and 92% for the year, outperforming the broad commodity index.* Our gold accounts, however, underperformed the index, up “just” 33% for the quarter. The primary reason for this gap is the high weighting we have to junior stocks which are only just beginning to move. As more interest comes to the sector, we expect money to trickle down to the juniors, which typically have strong moves when they do move. So we are maintaining our allocations, including in carefully selected exploration companies, looking for outperformance over the coming year and more.

■ The Fed finally moves in the face of the obvious

The Federal Reserve finally cut rates after holding steady all year in the face of the unavoidable conclusion that the labor market is not as “solid” as chairman Jerome Powell had emphatically asserted only weeks

earlier. That it was not so was obvious to anyone who looked beyond the headline unemployment rate or new jobs reports, obvious to anyone who appreciated that relying on monthly reports that typically had two wild revisions was making decisions on information that was a quarter of a year out of date (even before the massive annual revisions). The gap between the Bureau of Labor Statistics and ADP numbers…the increase in continuing unemployment claims…the reduction in the labor force…the high number of part-time jobs and so on: all these were, and are, indications that the labor market is far from "solid". We were not alone in pointing this out over the past year.

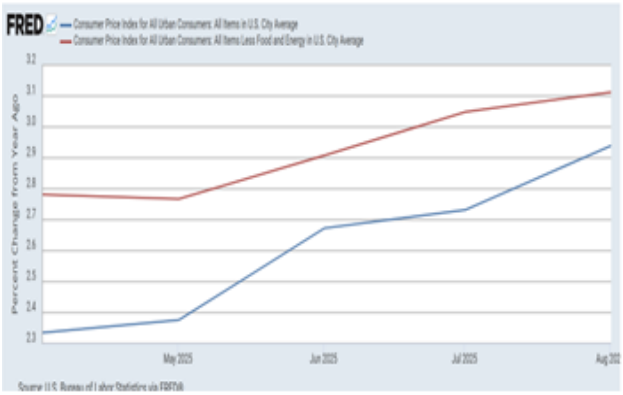
It is clear that the labor market is deteriorating, but equally that inflation (as commonly understood) is also stubbornly inching up, with the increases in consumer prices well above both where they were for more than a decade before covid as well as the Fed's own arbitrary target. There are those who suggest that the 45-year disinflationary trend, in place since Paul Volker killed inflation in 1980, is at an end, and a long inflationary period underway.

■ Consumer prices continue to inch up

The first part of that thesis is likely true, though arguably it is too soon to know with certainty about the second, but we do know that inflation tends to build on itself unless appropriate policy changes are made. To illustrate this, to buy goods valued at $100 in January 2020 now requires almost $192. So the value of the dollar has more-or-less halved during those five plus years, even though the CPI growth rate was less than 5% for most of that period.

Given the high growth in the Producer Price Index since the spring, it is pretty-much baked in that the CPI will move up in coming months. Powell has tried to push back against the narrative that September's rate cut is a precursor to more cuts ahead, but the odds favor further rate cuts. Beyond that, if President Trump wins his fight with the Federal Reserve then we shall likely see more rapid growth in the CPI in the coming years, just as we saw after Nixon fought and beat the Fed in 1971 and Johnson in 1965.

Inflation Moving Up Steadily



Higher inflation will have consequences for markets, most particularly for the bond market and for gold and other commodities. With the economy, particularly the labor market, deteriorating (albeit slowly) at the same time, then we are entering a period of stagflation, and such an economic environment also has clear winners and losers, if history is a guide. Winners include gold, oil, gold stocks, commodities, smaller market stocks and bonds; losers include U.S. and developed market bonds, U.S. and developed market stocks, especially big cap and growth stocks.

* Please note: **Past performance is no guarantee of future results.** For complete information on our past performance, including factors to be considered in viewing past performance and other disclosures, please contact our office. Specific stocks mentioned herein are intended solely as illustrative of strategies and types of stocks we are buying or selling, and are not intended as indicative of entire portfolios or of any individual client's portfolio. The numbers mentioned represent our composite averages. They represent all accounts that fall within the stated objectives which have the ability to buy and sell options; they exclude accounts under $25,000 and accounts with significant limitations or restrictions that would make them unrepresentative of the account type. Performance figures for composites reflect the deduction of administrative fees, but do not take into account any performance fee that may be charged for the period stated. The performance of any individual stock or stocks does not take into account fees. Performance numbers include dividends; dividends are not reinvested. Commissions charged may vary depending on the brokerage firm at which an individual account is held. All accounts are managed individually and are therefore different, even within the same broad objective. Factors such as an individual's circumstances, the size of the portfolio, and the time the account opened can affect specific buy and sell decisions. Factors such as price movements and security liquidity can affect whether any trade is made for all accounts. Global Strategic Management, an SEC-registered investment advisor, does business as Adrian Day Asset Management.

Most central banks around the world (with the major exception of Japan) have been cutting interest rates even before the Fed did, and before inflation has been conquered. Again, this risks unleashing a round of global inflation, such as we last saw in the 1970s.

■ Long slide in the dollar lies ahead

The dollar will also likely continue to decline, notwithstanding that it has already experienced its worst year-to-date decline in over 50 years, and a recovery bounce at least is overdue. All it could manage in the third quarter was a modest 3 pt rally, less than 25% of the decline, before dropping to new annual lows. But to the extent that the dollar loses its role as sole global reserve currency to that extent the dollar will decline in value.

The decline of the dollar as supreme reserve asset is underway. At the beginning of this century, 75% of central banks' foreign reserves were held in the U.S. dollar. A move to reduce that dangerous concentration in the face of a worsening U.S. fiscal situation, and later exacerbated by dollar weaponization, saw that percentage fall to around 65% five years ago, and thence to 48% this year. And this has occurred in the face of ongoing high dollar earnings by foreign countries as the U.S. trade deficit ballooned. This trend away from the dollar well pre-dated the current administration, though it is fair to say that nothing that has happened since January has lessened the desire of foreign countries, as well as foreign investors, to reduce dollar exposure.

If you are worried about single-asset concentration…if you are worried about the U.S. fiscal situation…and if you have concerns about dollar weaponization, is 48% of your reserves in the dollar still too much? This trend is likely to continue, though there will be counter-trend moves.

■ The U.S. stock market may be peaking

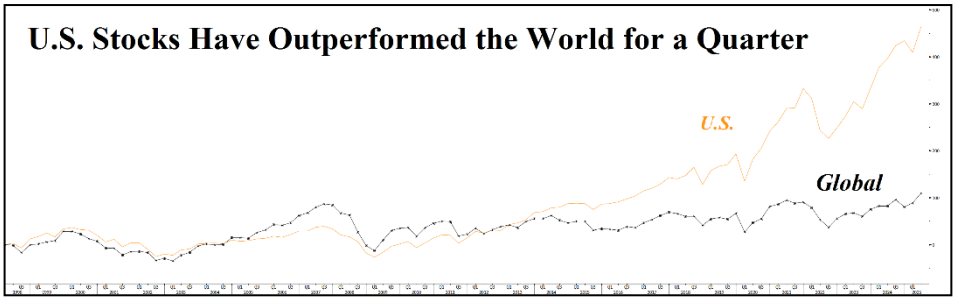
The direction of the stock market is the most difficult to gauge. In inflationary periods, stocks markets can do well when priced in their local currencies (*vide*, Zimbabwe and Venezuela). Ongoing money printing has to go somewhere and stocks, real estate, and collectibles are often destinations. On the other hand, the stock market overall has performed poorly in stagflationary periods, and there are many indicators that this current market is well overdue for at least a pullback.

- It is overvalued, on many metrics the worst since 1929, or even ever.
- It has narrow breadth, the worst in history; the "Magnificent 7" is now down to the "Magnificent 3" still driving the market higher.
- Insider selling to buying is at multi-decade highs.

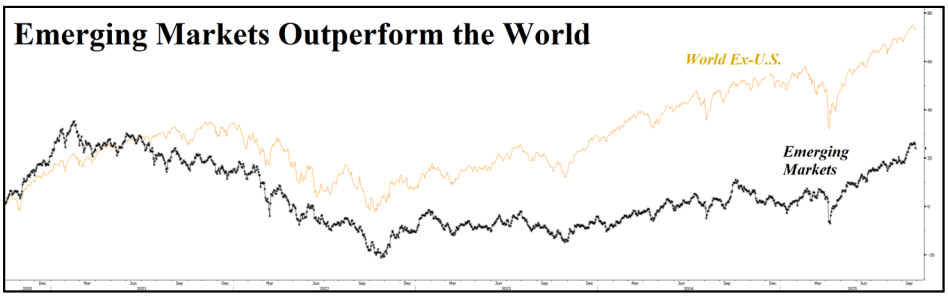
There are many other indicators we could cite that suggest the market is ripe for a fall. The Schiller CAPE ratio (which adjusts P/E for inflation and seasonal factors and is considered a better longer-term gauge) is at its second highest level in history. Margin debt in brokerage accounts just moved above $1 trillion, nearly double where it was five years ago; previous peaks preceded market crashes in 1974, 1987, 2008, as well as more recent declines). Meaningfully, margin debt-to-GDP is close to an all-time high, while the cost of carrying the margin is at a new high. In addition, there are large sums in leveraged ETFs that do not show up in the margin numbers, but are equally dangerous. And so on.

■ Caution is called for, and rotation

None of these indicators mean that the market must drop sharply and certainly not imminently—after all, the above was all true at the beginning of the year—but they are certainly warnings of the *risk* in the market. And today's high valuations tell us that future returns, from here, are most likely going to be low.



At the minimum, this calls for rotation out of the erstwhile leaders, such as U.S. growth, particularly anything to do with AI. Both in the U.S. and globally, value stocks are trading at historical lows relative to growth stocks. The Fama-French model shows that value stocks have outperformed growth stocks on any 10-year period back to the 1929 crash…until 2015. For the last decade, growth has dramatically and increasingly outperformed, leaving value stocks at their lowest level relative to growth in a century.



Equally, the U.S. has outperformed global markets by an ever-widening amount over the past quarter century, until this year, just as major markets have outperformed smaller markets. It could be time to rotate into value stocks and smaller market stocks.

■ Pullback could be close

There are other indicators, however, that suggest a top could be near. Jesse Felder, for example, points to rising volatility along with a rising index as a warning sign (as in 2008, 2020). He also points to the outperformance of consumer discretionary over consumer staples (as in 2000 and early 2022). Each of these periods saw S&P declines of varying magnitudes and timeframes.

We are reducing big-cap and growth stocks in developed markets, and looking for attractive buys among value stocks, smaller markets, and special situations. In addition, we continue to buy resources stocks.

■ The commodity sector is primed for a bull market

The broad commodity sector is trading just off 100-year lows relative to financial assets, as are commodity equities. That alone warrants a closer look. Commodity cycles tend to be long, and do not follow economic cycles, as one might expect. Rather, the typical commodity cycle, particularly for the resources, follows a pattern of overinvestment leading to overproduction leading to low prices, which in turn leads to restrictions on investment and production, leading to high prices, and the cycle starts again. Because the lag times between investment and production are long, and not in sync with the economic cycles, we often see low prices in strong economic environments and vice versa.

Right now, we are coming off a multi-year period of extreme under-investment, following the 2011-2012 binge. Low prices, investment just returning (but remember the long lag times to increase production), negative sentiment, and, in various sectors, signs of supply difficulties ahead: that is a combination ripe for higher prices and investment now. To illustrate how out of favor this sector is consider that energy used to represent 15% of the S&P while today, it's less than 3%.

As an additional factor, commodities generally also benefit from higher inflation, lower interest rates, and a weaker U.S. dollar, so the macro-environment is turning to one which generally favors this sector. Note, however, that a sluggish economic environment is a headwind to base metals and energy, though, as per above, not the dominant factor. It is however a factor that does not necessarily present a headwind to gold.

We are looking for investments across the spectrum, not only the metals, but energy and agriculturals as well. We favor commodities where there are signs of global depletion, but above all look for strong companies with solid balance sheets (to withstand further weakness and to grow without excessive dilution or debt) and proven management.

■ The popular narrative on oil & gas is wrong

We have been cautious on oil & gas, but increasingly turning more positive. The popular narrative is that the market is in surplus, that OPEC wants to boost output, that there will be large additions when the Ukraine war ends, that new offshore projects will boost supply, that demand is slowing, and that EV adoption will lead to a large decline in demand.

All of these assumptions, in our view, are incorrect. As demand continues to increase on the back of a reduction in EV adoption, while base supply declines offsetting new fields, the price will recover. Remember, the oil price today is less than half what it was at its 2011 peak, and meaningfully below where it traded for most of 2022-2024. We also think the sentiment on North American natural gas is overly pessimistic, because of fears of shale gas production irrespective of price. We are not looking for runaway prices any time soon, but the oil equities are priced for continued low prices. We see value in global integrateds, in large E&P independents, and in explorers.

■ Nothing has changed in gold demand framework

As gold finishes its best month in five years, the basic case for gold has not changed. As discussed above, the drivers of gold buying over the past three years have not changed, and in some cases have only accelerated. Importantly, the buyers and their reasons for buying are to a certain extent price agnostic, so the price can continue to move higher, well above trend. Of course, there will be periods when buying subsides, but more likely these will see consolidation rather than corrections, as, for example, we saw from mid-April to mid-August.

Gold is up 17% in the quarter just ending, all of it in the last six weeks, bringing the year-to-date gain to 46%. Silver is playing catch-up, with a vengeance, up 30% in the last quarter, and over 60% for the year so far.

“As gold finishes its best month in five years, the basic case for gold has not changed.”

Major establishment investors and investment firms are jumping on board, each, seemingly, trying to outdo the other. Goldman Sachs has $4,000 by mid-next year as a base case, but that is already looking outdated. The Financial Times had a headline suggesting gold would hit $5,000 “if Trump undermines Fed”. Remember, these are institutions and publications than only recently were ridiculing gold, with the FT calling it a “pet rock”, while Goldman, who had an end-2024 call for gold to hit $2,090 has continually revised their predications as gold has moved up. So to be honest, I do not put a lot of credence in these predications; if anything, they make the contrarian in me somewhat nervous.

To see sophisticated and successful investors calling for increased gold positions carries more weight. Ray Dalio is suggesting a 10% allocation in portfolios, while Jeffrey Gundlach, the “bond king”, called for a 25% allocation, with gold reaching $4,000 by year end. U.S. gold allocations now are well under 1% of portfolios, so we have a long way to go to reach these levels.

Meanwhile, Google’s worse-than-useless AI, in begging the question when it asks “why isn’t gold a good investment?”, answers “basically, gold has a low real return, i.e. the return after…inflation. It doesn't grow in the same sense a stock does nor does it produce dividends.” It sounds as though Google hired Warren

Buffet to write this! Gold bullion has appreciated by 1,250% this century, while the S&P has a return of just over half that, 629%, including dividends. Bet you are not hearing that on CNBC.

■ Gold stocks exhibiting leverage even as investors shun the sector

The gold stocks are beginning to exhibit their traditional leverage to bullion, with the GDX index up 49% in the last quarter. The juniors are beginning to move, with the Toronto venture index up 51% in the last three months, after being more-or-less flat for the first seven months of the year. Notwithstanding that these are great returns, we think the move in stocks is only just beginning.

Remember, North American investors typically turn to gold because of the economic environment, and that is only beginning to shift to one that is conducive to gold with a slowing economy, lower interest rates, higher inflation, and a weaker dollar. Although there have been some inflows into gold miner ETFs over the past month, the net flows are still negative, with $358 million of outflows over the past month, bringing the year-to-date total outflows to $3.8 billion.

■ Valuations still attractive

However, as the economic narrative shifts, even as the stocks continue to move higher amid record and growing cash flows, investors will increasingly turn to this sector. When that happens, the gold stocks will move even more dramatically higher, given just how small a sector this is.

And since the costs of mining have stayed relatively subdued as the price of gold has rocketed, the margins and therefore the cash flows have shot up, so on many metrics the stocks are still trading at valuations close to their long-term lows. Agnico Eagle, for example, though trading at a higher price-to-free cash flow multiple than where it traded at year end, is nonetheless trading at a lower multiple than it did for each of the other of the past five years, and has rarely traded lower over its 40-year history. So we remain very bullish on the gold stocks.

Overall, we continue to be cautious on most major global stock markets because of the risk, while looking for, and finding, value among smaller markets, overlooked situations, and resources, continuing to hold a high allocation to gold.

Review of Individual Accounts

■ Global accounts

Our global accounts have increased cash over the last quarter as we continue to trim positions as global markets get more stretched. Our mid-risk accounts now hold over 6% in cash (and cash equivalents), up from 2% at the end of the last quarter. More conservative accounts hold higher levels.

Our overall allocations remain broadly similar to where we entered the quarter, with Hong Kong, Singapore, Britain, and the U.S. being the markets with the highest exposure—though we are significantly underweight the U.S. —while gold, resources and the Business Development Companies are the sectors with the highest allocations.

We are trimming on rallies and adding to favorites

Most of our selling this past quarter was reducing specific stocks on rallies; this included gold stocks for more conservative investors, even as we maintain allocations. We exited only one stock: a Chinese internet company after a strong rally made it no longer undervalued. (The SEC does not like us to name specific stocks.)

On the buy side, we added one more U.K. company that has strong growth potential and is a possible acquisition candidate. This is a soft drinks manufacturer that has recently entered the North American market in a major way with an investment from a U.S. company. We also added to a few stocks on individual weakness.

We have also started selling puts on a couple of depressed U.S. companies that appear ready to turn around. We will either have the stocks put to us, or pocket the premiums. We are also taking a few positions that will benefit from market declines, including on the VIX volatility ETF.

Looking ahead, we expect to see cash holdings increase as markets continue to get ever-more stretched in valuations. At the same time, we search the globe, as ever, looking for quality companies selling at good valuations, including stocks that decline on what appear to be temporary factors. And we continue to hold high allocations to gold and other resource stocks, even as we trim overweight positions, particularly for more conservative investors.

■ Gold Accounts

The gold accounts have seen some shifts, partly from our decisions and partly from market moves. The allocation to senior companies increased significantly over the quarter from 26% to 32%, even as we trimmed holdings in this sector. The reasons were two-fold: first, a widely held junior was acquired by a senior company, and we received shares; second, the seniors had greater moves than the juniors.

The exposure to junior and exploration stocks declined somewhat (from 35% to 31%) largely for the same reasons that the senior allocation increased; we "lost" our most widely held junior company in an acquisition. Cash increased to 5%, but this is somewhat deceptive. Most of the cash is set aside for buy orders, while new accounts in the last week are not yet fully invested.

Cash influx reinvested across the board

We did receive a large influx of cash at the beginning of the quarter in the transaction referred to above. We received essentially half cash and half shares from the acquiring company. That cash was quickly reinvested.

We started buying another major miner, meaningfully undervalued relative to the others, that is making great strides at turning around costs and the balance sheet. We also added to a major royalty company, taking advantage of a decline in the stock price after it announced an acquisition (as often happens). We also purchased a new intermediate miner, which recently acquired an operating mine from Newmont in addition to a mine in Mexico, and is developing a third; we bought when Newmont sold its shares in the company at a discount, taking the stock price down.

In addition to that, we started buying a few new junior companies for appropriate accounts, and added to some of our favorites that remain attractively valued or where we expect near-term catalysts. Among these are a pair of companies that are merging in a high-profile transaction.

We exited only one company, a smaller producer that stumbled seriously on ambitious growth plans. Though it may come out the other end, we decided to raise some cash and look for another opportunity to re-enter the company after the balance sheet has been fixed.

Looking ahead, we expect to continue to be fully invested, even as we take some profits and reinvest in new situations. We expect the allocation to juniors to increase as the smaller companies start to catch up with the larger ones.

Resource Accounts

Resource accounts also remain essentially full invested, with cash mostly set aside for buy orders. We continue to have highest weightings in gold, copper, silver and broad-based exploration, though are slowly building positions in oil & gas. The exposure to senior gold stocks increased, even as we trimmed positions on rallies to raise cash for other investments. This was due to the outperformance of that sector, as well as the addition of a new holding with the acquisition discussed above under "Gold Accounts".

We have not exited any positions in the last quarter but have added a few. We have bought a new Canadian oil exploration company that sports an attractive dividend yield; another company active in the prolific Vicuña belt in the southern Andes; a new company acquiring a prospective former gold mine in Nevada (still private); and a newly listed Peru copper explorer (that we held for some clients as a private company).

Going forward, we expect to remain fully invested, as we trim senior gold stocks (and others) that have done particularly well, maintaining our allocation but providing cash to invest in other sectors, particularly silver, oil & gas, and uranium. We expect gold to remain our largest weighting, given its strong risk-reward profile.

In sum, stretched valuations and heightened uncertainty are leading us to reduce exposure to major stock markets. The continuing move away from the dollar as the supreme reserve asset, as well as policy changes in the U.S., will see higher inflation and a weaker dollar, with obvious implications for markets. Prime among those is a possible resurgence in commodity markets. In addition to high exposure to these markets generally, and in particular to gold, we continue to look for, and find, quality, undervalued situations on a bottom-up basis in global stock markets. The rest of the year promises increased volatility and heightened risk, but with that, great opportunities for gains.

Adrian Day, September 30th, 2025

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