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MONTHLY



*Global Investment Letter*



### **Notable Inside This Issue:**

- *The Tariff Man Cometh*
- *Waiting for Nasdaq Confirmation to Buy S&P 500*
- *Half Position in FTSE 100 Purchased*
- *We're Still Short 10-year Treasury Notes*
- *The Dollar is Expected to Move Higher*
- *We Continue to Hold Our Short Position in the Canadian Dollar*
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## THE TARIFF MAN COMETH

The obvious “elephant in the room” that demands discussion this month is the launch of a trade war by President Trump that has begun with the imposition of punitive tariffs against Canada, Mexico, and China. We have expected, and he recently confirmed, that he intends to extend his trade war to Europe in 2025. We anticipate Japan and other nations will eventually be drawn into the trade war, making it a global trade war.

We will refrain from addressing the political or moral implications of President Trump’s actions and restrict ourselves to the consequences for investors, as that is the mandate of this publication.

As students of history, we have learned the great benefits derived from free trade and the perils of government meddling in markets. The negative effects of restrictions on trade, such as tariffs, are unequivocal. We included an analysis of the historical effects of tariffs on the American economy in our December issue, and rather than have readers refer to the December issue, we believe this requires rereading and have included it below.

## A HISTORY OF U.S. TRADE TARIFFS

Trade tariffs have historically played a significant role in shaping the economic and market landscapes of countries. These duties imposed on imports are meant to protect domestic industries by making foreign goods more expensive, thereby encouraging consumers to buy locally produced products. However, the impact of tariffs can be complex, often leading to both positive and negative consequences for economies and markets.

In the early 19th century, the Tariff of 1828, also known as the “Tariff of Abominations,” was one of the most controversial tariffs of the period. It led to significant regional tensions, especially between the industrialized North and the agricultural South. The South viewed the tariff as an instrument of plunder and theft, as it increased the cost of manufactured goods. The regional animosity produced by this tariff has been seen as a contributory factor to the eventual Civil War, though slavery was the central issue of that conflict.

Late in the 19<sup>th</sup> century, the McKinley Tariff (passed on October 1, 1890) was a major piece of legislation that raised the average tariff on imports to almost 50%. It was a protectionist measure supported by the Republican Party and was a major topic of debate in the 1890 Congressional elections. The McKinley Tariff was unpopular from the outset, as it featured selective tariffs in which rates were raised on some goods and lowered on others. This allowed for an environment of corruption to flourish as various business interests lobbied for a favourable status for their products. The unpopularity of the tariffs contributed to the Republicans losing the Presidency to Democratic candidate Grover Cleveland in 1892. The Dow Jones Index did not fare well during the McKinley Tariff era. The Dow experienced a decline of 14.2% in 1890, a

rebound of 17.6% in 1891, a decline of 6.6% in 1892, a significant decline of 24.6% in 1893, and a further decline of 19.4% in 1894. The McKinley Tariff was eventually replaced by the Wilson-Gorman Tariff Act in 1894, which lowered tariff rates. The McKinley Tariff exacted considerable damage to the U.S. economy and stock market.

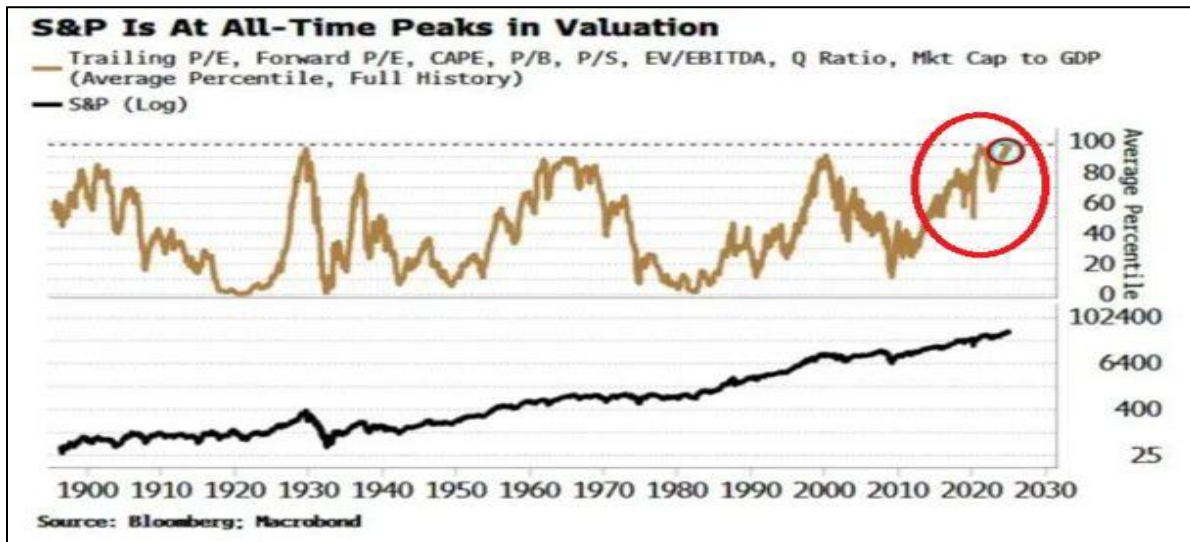
The Smoot-Hawley Tariff Act of 1930 provides a stark example of the adverse effects of high tariffs. Implemented during the Great Depression, it aimed to protect American jobs and industries by raising tariffs on over 20,000 imported goods. However, it led to a significant reduction in international trade as other countries retaliated with tariffs of their own. The resulting trade war exacerbated the economic downturn, contributing to a deeper and more prolonged global depression.

More recently, the imposition of tariffs during the U.S.-China trade war beginning in 2018 has had significant effects on global markets. The U.S. levied tariffs on billions of dollars worth of Chinese goods, leading China to retaliate with its own tariffs on American products. This trade conflict disrupted supply chains, increased costs for businesses, and created uncertainty in global markets. Despite intended protections for domestic industries, certain sectors like agriculture suffered due to reduced access to key export markets.

While tariffs can protect domestic industries in the short term, they often lead to higher prices for consumers and strained international relations. Moreover, retaliatory measures from trade partners can hurt exporters and broaden economic growth. Historical examples show that while tariffs may offer temporary economic shelter, they frequently result in unintended negative consequences, highlighting the delicate balance policymakers must maintain in crafting trade policies.

### **U.S. STOCK MARKET VALUATION AND SENTIMENT**

The catalyst for market volatility provided by the trade war is set against an investment landscape that is vulnerable to developments that shake the very bullish narrative that has been embraced by consensus opinion and reflected by markets.

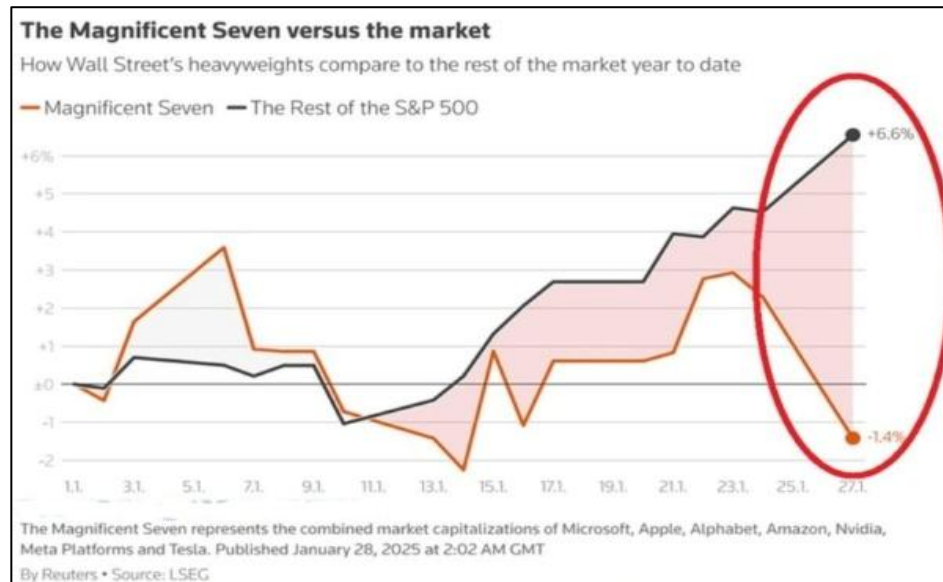


The S&P 500 valuation rests at all-time highs, with a perusal of previous valuation peaks on the chart above suggesting the prospects for a further expansion of valuation and continued strong performance by stock markets is unlikely.

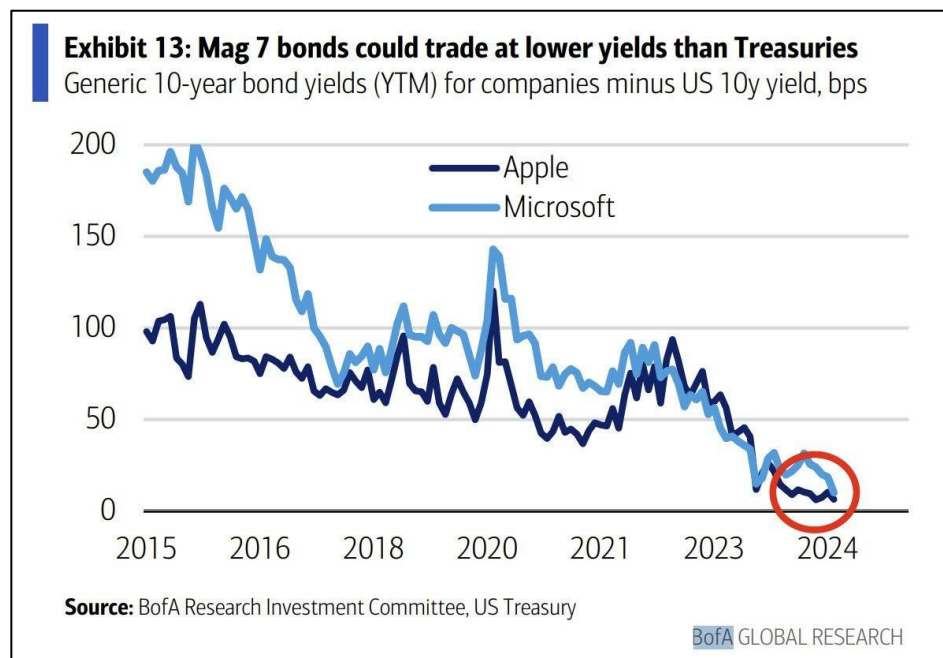
We have commented previously on the importance of paying attention to the relative performance of market leaders, currently the “Magnificent 7”, for clues of future market behaviour. This has proven to be a reliable indicator throughout our career in money management, with the poor relative performance of the FAANG+ group in the second half of 2021 heralding the market retreat of 2022.

The chart on the following page demonstrates that January has not been kind to the performance of the “Magnificent 7” versus the broader market. A major influence on the poor relative performance was the sharp decline of Nvidia in response to the commercial introduction of rival DeepSeek. The weakness of Nvidia is especially noteworthy in this historically narrowly led market, with Nvidia alone accounting for over 22% of the S&P 500’s total appreciation in 2024. The weakness demonstrated by the “Magnificent 7” raises the probability that the current bull market is approaching an end.

We have seen the cycle of poor relative performance of market leaders evolving into a bear market, with a new group of companies emerging as leaders of the next bull market.

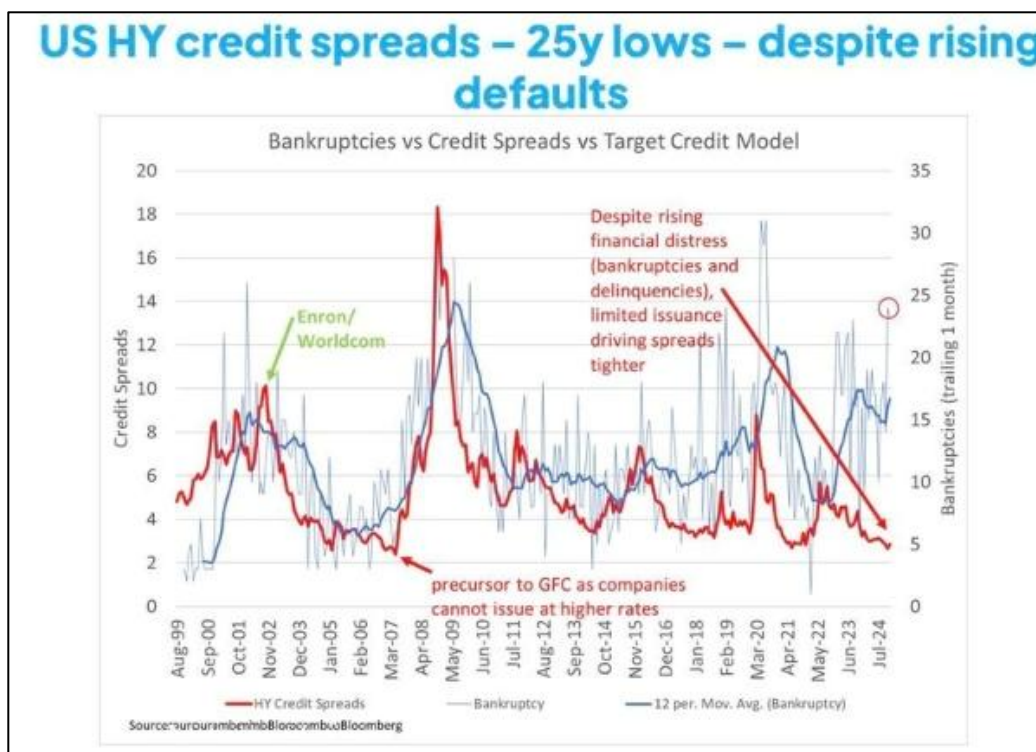


Where we are today in this market cycle will depend on the state of investor optimism, which remains at a very high level as reflected by the following chart.



The bonds of Apple and Microsoft are currently trading with almost the same yields accorded to U.S. 10-year Treasury Notes, which are considered the closest thing to a risk-free investment given that they are backed by the U.S. government! While Apple and Microsoft are financially very strong and certainly wonderful businesses, we do not believe any private company should be viewed as almost risk-free given the basic systemic risks of being in any type of business. That these companies are implicitly viewed this way is a comment on what we believe is an almost delusional level of optimism on the part of investors.

The very sanguine view of the corporate bond market is not restricted to companies with the highest creditworthiness, as the following chart illustrates.



U.S. high-yield (junk) bonds are trading at their lowest spreads versus high-quality bonds in 25 years despite a rising trend in defaults. The previous peak in optimism (or complacency) on the prospects for junk bonds appeared, rather ominously, not long before the bursting of the Internet Bubble.



## THE CURRENT INVESTMENT ENVIRONMENT

Our forecast for the 2020s, since the late 2010s, has been that it will be a decade known for its market volatility. Our view was based on a confluence of economic and geopolitical factors that would provide a slew of potential catalysts for volatility, with at least some fulfilling their potential. Thus far, this decade has met our expectations for volatility, with the appearance of a pandemic and the end of a 40-year-long decline in global interest rates that saw much of the developed world adopting negative rates.

More catalysts for volatility stand waiting in the wings, with the latest one appearing in the form of a trade war initiated by President Trump. A trade war is perhaps the most serious of all threats because constricting trade has proven to be the surest route to stifle economic growth. It has always been so, as described in Eric Cline's book, "1177 BC: The Year Civilization Collapsed," which recounts the decline of trade in the Mediterranean region.

The financial markets may prove to be a brake on Trump's more unsound economic policies. The rise in yields on U.S. 10-year Treasury Notes since September is an indication that the bond market has reservations about tariffs and a number of his other policies. If the stock market responds negatively to the launch of the trade war, we may see a pullback on the implementation of tariffs. With mid-term elections less than 2 years away, Trump cannot risk a repeat of the weak stock markets that previous American tariff policies have produced.

However, Trump has been advocating the aggressive use of tariffs in interviews since the "Art of the Deal" days of the 1980s. However misguided, it is a strongly held core belief of his, and as such, he is unlikely to give up on the notion lightly, suggesting that any pause in the implementation of tariffs may only be a delay rather than an all-clear message for markets. If Trump does not repudiate the use of tariffs, the threat will hang over markets, creating investor uncertainty.

In the current environment, the volatility created by any catalyst will be magnified by both the elevated valuation of U.S. equities and the striking level of investor optimism that exists, not only in the U.S. but in other major stock markets (e.g., the German Dax Index has recently broken out to new highs). We fail to see how this combination of factors will not produce a good deal of market volatility going forward.

Our current investment stance remains defensive. Our short positions in the Canadian dollar and 10-year Notes (which represented our only two positions at the end of the 2024 year) are both profitable. We purchased new positions in gold, the FTSE 100 and the ITA ETF in January, with all off to a positive start. We draw subscribers' attention to our discussion of the silver market, which bears watching and carries the potential to eventually produce a significant bull market.

The volatility we expect will be challenging but will also be a source of great opportunities.

## EQUITIES COMMENT

### S&P 500 (WEEKLY)



We remained on the sidelines of the S&P 500 market in January, in part to seek clarity on the Trump Administration's intentions on tariffs, but primarily because we did not receive confirmation of a new market rally through the establishing of a new price high by the Nasdaq 100.

Experience has taught that the Nasdaq typically leads the other major U.S. indices in both bull and bear markets. It does so because of its high weighting in technology and growth stocks from which almost all market leaders are derived.

This is certainly the case in the current market environment, with the extremely narrowly led S&P 500 dependent on the fortunes of the “Magnificent 7” group. Indeed, there were times when the S&P 500 relied on just one stock, Nvidia. The sharp pullback by Nvidia in January should serve as a reminder that no stock should be viewed with complacency and that rapid change is endemic to the technology sector.

We are prepared to purchase a new full position in the S&P 500 upon the Nasdaq 100 making a new price high, which would represent very bullish price action. If a purchase is made, we will set our initial protective sell price 2-3% below the previous market high to guard against a failed breakout attempt.

## HEALTH CARE TRADE

### HEALTH CARE SPDR ETF (XLV) (WEEKLY)



Health care stocks, as reflected by our proxy for exposure to the sector, the XLV ETF, rallied smartly in January and now trades bullishly above both its 10 and 40-week moving averages.

XLV benefited in January from a market rotation into more defensive sectors in anticipation of the potential consequences of a trade war and weakness on the part of some members of the “Magnificent 7”, most notably Nvidia.

While the rally last month must be considered positive, an unambiguous buy signal has not been given. The technical damage to XLV during the recent decline and the events of January have not completely repaired the situation. We would have preferred to see a bullish reversal bar in late 2024 that would have indicated a peak in negative sentiment resolving into a change of trend. The absence of a reversal bar casts some doubt on the durability of the recent rally.

The major bearish reversal bar last fall that started the downtrend in XLV represents major technical resistance. We will wait until XLV trades through that bar before again purchasing a position. The risk/reward prospects of buying at current levels are not sufficiently attractive.

We expect our patience will be rewarded with a new buying opportunity in health care, a sector on which we remain firmly bullish for the long term and which has been a source of attractive profits in the past.

## FTSE 100 (DAILY)



As we wrote in the last issue, *"We remain prepared to buy or sell the FTSE upon a breakout above or below the current price channel."*

Somewhat to our surprise, the London FTSE broke out of its extended trading channel and we duly bought a half position in the index at 8505. We set our initial protective sell price at 8375.

The bullish move by the FTSE in January is likely the result of several factors. Consensus opinion has embraced the notion that Britain will not be a target for American tariffs (to which we do not necessarily subscribe) and that interest rates will decline sharply in 2025. As well, the recent weakness of the pound has made British exports more price competitive, which helped the shares of exporters. Finally, the FTSE benefited from a rotation from technology to the mining and oil sectors, which are heavily weighted in the index.

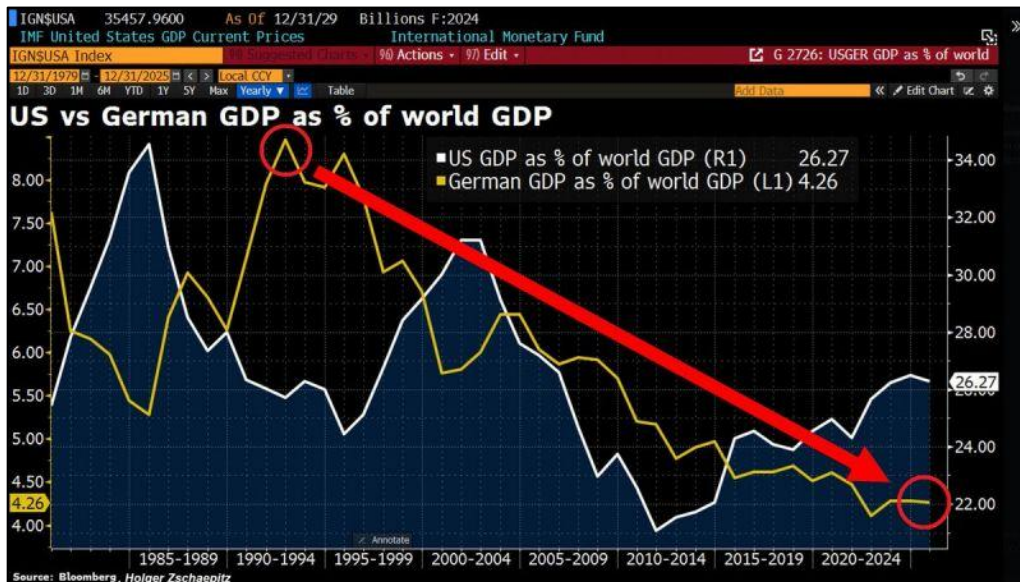
Our decision to purchase a half rather than full position in the FTSE reflects our caution on what are currently believed to be non-U.S. targets until some clarity on the scope of Trump's tariff ambitions can be understood. Nonetheless, the breakout from the technical pattern displayed in the FTSE chart is very bullish and cannot be easily ignored.

The risk/reward proposition offered by this position is very attractive, considering the upside potential versus the small amount risked by buying a half position and employing a protective sell price.

## DAX INDEX (WEEKLY)



The Dax index sailed to new heights in January, with export-dependent Germany responding positively to the recent weakness of the euro versus the dollar. We can think of no other reason, for the German economy contracted 0.3% in 2024 following a 0.1% decline in 2023. It is an economy in de facto recession and one that has seen its global influence shrink over the years, as the following chart depicts.



Perhaps a more pointed threat to the German economy rests with our expectation that the Trump administration will eventually turn its tariff ambitions to Europe, and especially to the German auto sector, which produces only 38% of the vehicles sold in the U.S. in that country.

The Dax reflects a bullish worldview that we do not share. While we normally buy major price breakouts as a matter of course, we find ourselves in a similar mindset to that of February/March 2020 when we believed that U.S. and global markets did not reflect the threat posed by COVID and recommended selling equities in favour of Treasury bonds.

Subscribers can view our thoughts at that time in the February and March 2020 issues posted on our website. Our warning at that time prevented ourselves and others from experiencing the March 2020 market crash. While we don't expect the DAX to drop to the same extent as 2020 on the announcement of U.S. tariffs, we hardly think the news will be received well.

Trump has yet to announce tariffs against Europe, and perhaps he won't. But we believe he is highly likely to do so and prefer not to risk being right. The reaction to a tariff announcement may produce a buying opportunity in the Dax, for which we will be watching.

## CAC 40 (WEEKLY)



The Paris Cac 40 Index rallied strongly in January, and like the Dax, we attribute the rise in good part to the trade benefits of a weaker euro against the dollar.

The uncertain geopolitical scene, i.e., the potential of a U.S. tariff war with Europe, and the proximity of the Cac 40 to major technical resistance represented by the 2024 price high, makes for a less than compelling risk/reward proposition for this market.

As with the Dax, we choose to remain on the sidelines of this market.



## NIKKEI INDEX (WEEKLY)



The Nikkei continued to trade in a relatively narrow channel, exhibiting no clear trend.

Given the lack of trend and uncertainties associated with tariffs and the global economy, we remain on the sidelines of this market for the time being.

## SENSEX (WEEKLY)



The Indian Sensex Index declined sharply in January before mounting a recovery in the last week of the month on optimism about the contents of the Union Budget to be announced by the finance minister on February 1.

While our long-term optimism on the future of India remains intact, we still view current exposure to Indian equities as being less than compelling from a risk/reward standpoint.

From a technical standpoint, the Sensex is now trading bearishly beneath both its 10 and 40-week moving averages.

From a geopolitical standpoint, India is a prime target for American tariff attention, as India has employed significant use of tariffs through the years to protect its domestic economy.

We will wait until more clarity is available on American trade policy before venturing into the Indian market once again.

## EMERGING MARKETS ETF (EEM) (WEEKLY)



As we commented in the January issue, *"The strong inverse relationship between the value of the U.S. dollar and emerging markets continued to assert itself in December, pushing our proxy for the sector, the EEM ETF, lower."*

The dollar retreated in January, which resulted in a rally by EEM. However, given our expectation that the rally by the dollar will resume and that major emerging markets (aside from China) may be targets for American tariffs, we will remain on the sidelines with these markets until an attractive buying opportunity is presented.

## FIXED INCOME COMMENT

### 10-YEAR US TREASURY NOTE (WEEKLY)



Our short sale of a full position of 10-year Treasury Notes at 108.9 in December recorded a small paper loss at the month-end January price close of 109.1.

After declining smartly in December and early January, the 10-year Notes rallied off of the technical support offered by the mid-year 2024 price low at circa 107.5. A weaker-than-expected GDP report raised expectations that a slowing economy would ease upward pressure on long rates by easing inflationary pressures (which remain above the Federal Reserve's 2% target).

Offsetting this seeming bullish news for the 10-year Notes was the announcement by President Trump of the imposition of 25% tariffs on a broad range of imported goods from Canada and Mexico. An additional 10% tariff was added to existing imports from China.

We expect the various import tariffs to prove inflationary, especially the tariffs applied to the substantial amount of oil imported from Canada (the tariff on Canadian oil has been placed at 10% to limit the inflationary effect, which will still be material).

We do not think Trump will restrict his imposition of punitive tariffs to the countries mentioned above as 2025 progresses. We believe that Europe and Japan remain prime targets. Further tariffs will stoke inflationary pressures.

We continue to believe that the path of least resistance is for higher long-term yields (lower Treasury prices) and are content to keep our short position in place. However, we will adjust our protective buy price upward from 109.25 to 109.6 to provide this position with a bit more “wiggle room.”

Trump’s imposition of announced tariffs, and the prospect of more to come, raises the probability that we are entering a period of global economic stagflation similar to that experienced in the 1970s. Tariffs will put upward pressure on inflation, while the constriction of global trade due to the tariffs will serve to slow economic growth.

Our expectation of rising odds for stagflation is in keeping with the following chart, which suggests that we have embarked on a secular trend of higher interest rates following the historic bull market that unfolded following the peak of interest rates in the early 1980s.



We could be wrong, and this secular trend in rates may not transpire (which is why we have our protective buy price in place), but history suggests that when governments meddle with free markets (as with tariffs) good things seldom happen.

## CURRENCY COMMENT

### US DOLLAR INDEX (DXY) (WEEKLY)



The U.S. Dollar Index pulled back in January following the sharp rally from the October low before exhibiting renewed strength late in the month as it became increasingly apparent that the Trump administration was intent on implementing the previously threatened tariffs against Canada, China and Mexico.

The imposition of these tariffs, along with our belief that they will be followed by more tariffs against other nations, suggests that the Dollar Index will resume its rise. The next major area of technical resistance sits at circa 114, which is our current price target for the Dollar Index.

As we've recounted previously, we believe the dollar's rise in response to the imposition of tariffs will be due in large part to the efforts of America's trading partners to devalue their currencies to mitigate the pernicious effects of tariffs by making their exports more price competitive. Along with retaliatory tariffs, currency devaluation is the historical response to the declaration of a trade war.

For this reason, and for the strength the dollar will derive from its role as the world's reserve currency in increasingly fraught economic and geopolitical times, the dollar may well rise more sharply than many expect.

## CAD/USD (WEEKLY)



Our short sale of a full position in the Canadian dollar in December continues profitable, with the dollar ending January at .695. As a consequence, we are lowering our protective buy price from 71.25 to .7050, which guarantees a solid profit on the position.

Our expectation that the Bank of Canada (BOC) would seek to cushion the blow of expected American tariffs was met in January with a 25-basis point reduction. While lower rates are stimulative to the economy, they most pointedly serve to weaken the Canadian currency versus its American counterpart. We expect to see further rate cuts (and efforts to weaken the Canadian currency) in 2025 if the trade war remains unresolved.

## EUR/USD (WEEKLY)



The European Central Bank (ECB) cut interest rates a further 25 basis points on January 30th, bringing the deposit facility rate to 2.75%. The ECB has now cut rates 4 times in the past year.

The late January rate cut by the ECB, given that the Federal Reserve kept rates unchanged at its meeting last month, served to reverse the rally enjoyed by the euro since the start of the year by making the interest rate differential with the dollar less favourable.

The ECB has been fairly aggressively cutting rates over the past year to combat an economy flirting with recession, while inflation remains stubbornly above the 2% target.

We suspect the interest rate actions of the ECB are, at least in part, an effort to weaken the euro in anticipation of eventual American tariffs. Further rate cuts in 2025 can be expected.

We have long been skeptical about the long-term viability of the euro, with the establishment by the European Union of a common currency without a common treasury to manage the economy being a fatal flaw.

We expect further weakness from the euro, with the decline accelerating if American tariffs are announced. Major technical support exists at the 2023 price low, which is a likely downside target.



## POUND/USD (WEEKLY)



The British Pound rose against the dollar in January, which we suspect owed more to the decline of the dollar in response to a weak GDP number and hopes that tariffs will be avoided than to the particular merits of the British currency.

The Bank of England (BOE) commenced cutting interest rates in August, implementing a 25 basis point reduction to 5%. It then followed with a further 25 basis point cut to 4.75% in November. However, the BOE decided to forestall further cuts in December amid concerns about rising inflation.

The BOE is presented with a difficult economic landscape. The British economy is sufficiently weak to deserve the stimulative effects of a further rate cut, but inflation in Britain is proving intractable, with a further rate cut risking further fueling of the fires of inflation.

The upcoming BOE meeting on February 6th is likely to see another 25 basis point rate cut. While inflation is a continuing problem, addressing the slowing economy seems top of mind for BOE officials. As well, the lack of easy access to a large market to sell exports, as a result of Brexit, makes a lower pound, which can be facilitated with a rate cut, desirable.

Given our bullish expectations for the dollar, our anticipation of a lower pound is not surprising. We expect to eventually see a return to the price lows of 2023.

## YEN/USD (WEEKLY)



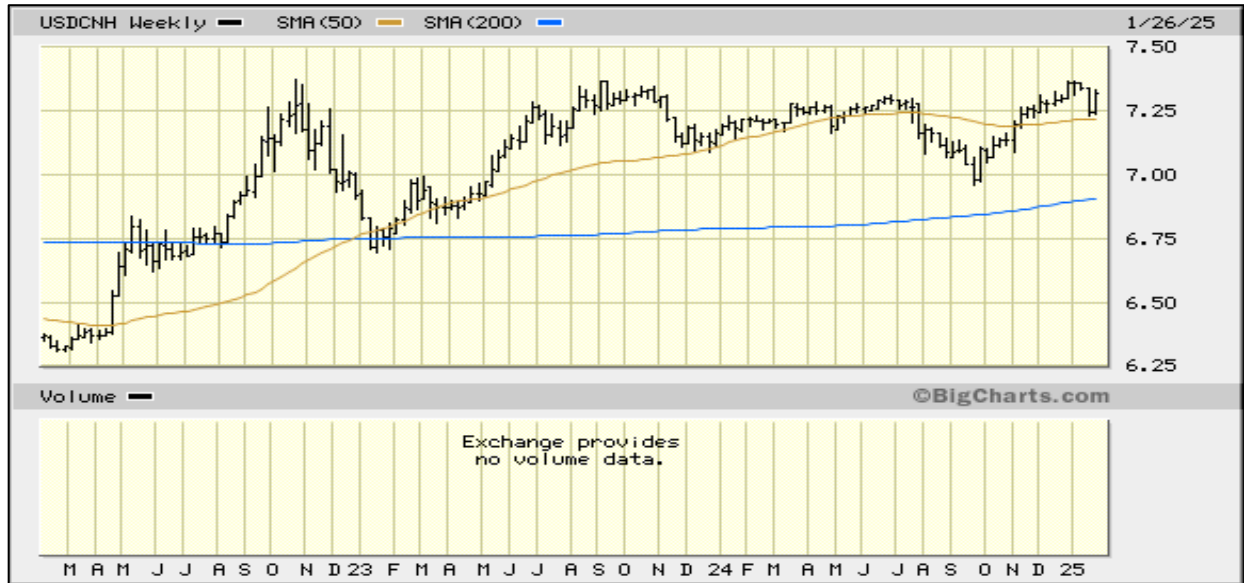
The yen strengthened in January in response to an interest rate increase by the Bank of Japan (BOJ) of 25 basis points to bring the key interest rate to 0.5%. The general weakness of the dollar contributed to the yen's rise.

Contrary to most other central banks, the BOJ is raising rates as part of a broader effort to normalize monetary policy after an extended period of negative interest rates and market intervention that served to distort the Japanese financial landscape. The BOJ has discontinued its policy framework known as Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control (YCC), which has been in effect since 2013.

The BOJ appears intent on raising its key interest rate to 1.5% over time as a means of combating inflation (which remains above 2.5%) that is being supported by upward pressure from wage growth.

A continued gradual strengthening of the yen is expected, with a couple of important caveats. American tariff actions against Japan would likely be met with a devaluation of the yen. Also, the long-standing inverse relationship between the Nikkei and the yen suggests that significant weakness by the Japanese stock market would likely result in actions by the BOJ to weaken the currency.

## YUAN/USD (DAILY)



The Chinese yuan continues to hover near major technical support at circa 7.35. We have suggested that Chinese authorities would wait until American tariff intentions are known before a decision on devaluing the currency is made.

On February 1, the Trump administration levied an additional 10% tariff (over existing tariffs) on Chinese imports. It remains to be seen if a 10% increase is sufficient to prompt a devaluation.

We remain of the view that a weaker yuan would be in China's interest given the slowing economy as it would be a means of spurring its still important export sector.

## OIL COMMENT

### CRUDE OIL (WTI) (WEEKLY)



The price of WTI posted another increase in January, fulfilling our view in recent months that the odds favoured higher prices as it rebounded from trading close to major technical support.

Notwithstanding the expected bump from the 10% tariff President Trump has levied on the 4 million barrels imported from Canada each day, we believe most of the upside potential in the price of oil has been exhausted (with our usual caveat that geopolitical events could provoke a spike in prices).

The global demand picture for oil remains troubling, with notable economic slowing in the European Union and China. The lack of significant growth in oil demand from China is particularly challenging to higher oil prices, as China has been the major driver of oil demand growth for the past 30 years. Finding another major source of demand for the coming decades will be difficult, with India being the most likely candidate. Maintaining oil demand growth at a healthy level in the decades ahead will be very challenging, with forecasts of rapidly declining populations in many countries and the increasing availability of alternative fuel sources pointing to lower, rather than higher, demand.

The path of least resistance for oil prices in 2025 is probably lower, barring adverse geopolitical developments.



The rally attempt by our proxy for exposure to oil & gas equities, the XLE ETF, that began in December ended in early January, with XLE surrendering most of its gains for the month.

XLE is now trading bearishly below both its 10 and 40-week moving averages and faces considerable challenges to the upside given the less-than-robust prospects for oil prices and equity markets.

XLE has been the source of a series of very profitable transactions, most recently through our profitable sale of a position at 92.25 in December, and we expect it to again offer an attractive buying opportunity.

However, we are currently content to remain on the sidelines of this market until such an opportunity is presented. A price breakout above the 2024 price high would be a bullish development and prompt us to establish a new position, placing our initial protective sell price 2-3% below the 2024 high.

## DEFENCE SECTOR COMMENT

### US AEROSPACE & DEFENCE ETF (ITA) (WEEKLY)



We wrote in the last issue that we expected to once again establish a position in the defence sector, which has been a core investment theme since the first issue of the Global Investment Letter and a source of handsome profits in the past. The price breakout by our proxy for the sector, the ITA ETF, has prompted us to purchase exposure to the defence sector rather more quickly than we had expected.

We established our position at 158.25 and have placed our initial protective sell price at 153, which is just below the bottom of the January gap-up bar that we consider a source of technical support.

The geopolitical and technological reasons for our enthusiasm for the sector seem to get stronger by the day. U.S. insistence that Europe spends more on its defence (a reasonable request) will result in a considerable increase in defence spending by the European Union (as we highlighted in the last issue). The combination of diminishing confidence in America as a defence partner and concerns about further Russian territorial ambitions can be expected to provide strong motivation for European defence spending in the years ahead.

Russia is considered a major threat by Europe, as illustrated by the chart on the following page, which demonstrates that defence spending tends to increase with a nation's proximity to Russia. We do not think this is coincidental.



The rapid development of technology is also an ongoing source of demand, with moves to incorporate Artificial Intelligence into digital weapons systems being the latest innovation.

We continue to believe that focusing on defence companies producing weapons systems of the highest technology, such as aerospace and related products, is the optimal strategy.

We expect the Trump administration to continue distancing itself from NATO, which could alter the buying patterns of European nations. For that reason, a measure of geographic diversification among defence holdings may be warranted.

Major European companies worthy of consideration are BAE Systems, Dassault Aviation, Rheinmetall AG, Airbus and Thales Group.

In the U.S., we continue to favour Northrup Grumman, Lockheed Martin, General Dynamics, Boeing, and Raytheon Technologies (all of which are heavily weighted in ITA).

## GOLD & SILVER COMMENTARY

### GOLD (WEEKLY)



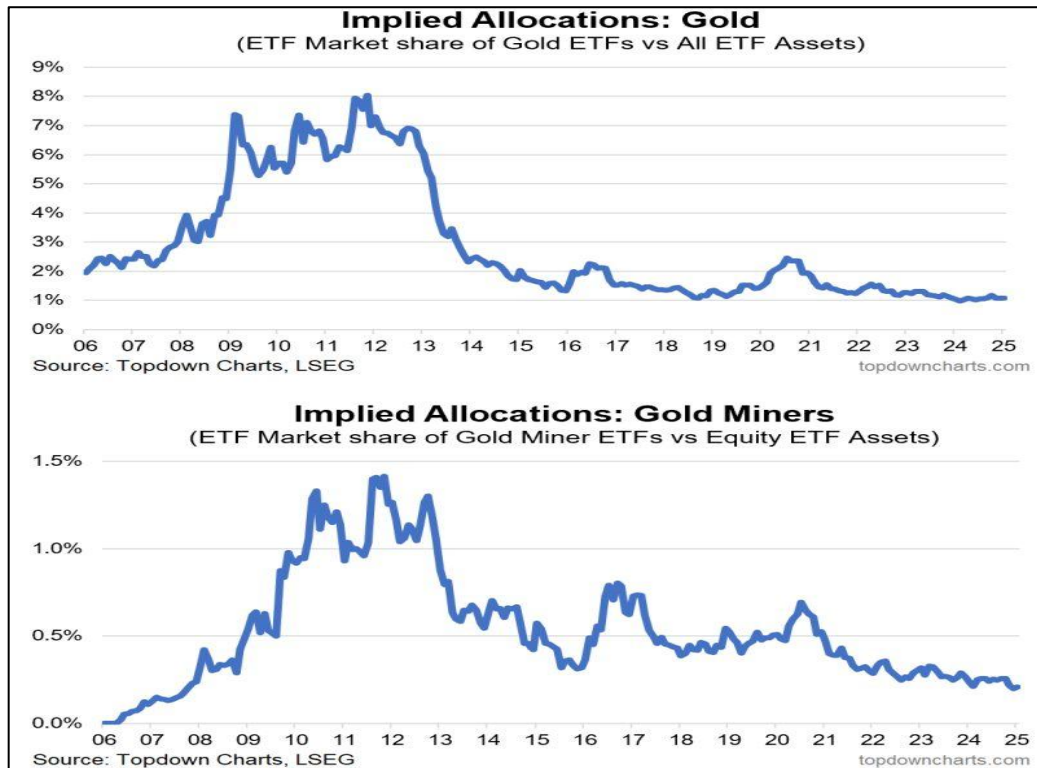
The price of gold rose to a new all-time high in January, which prompted us to establish a new full position (as is our custom with important price breakouts) at \$2805. Our initial protective sell price is set at \$2740. The gold market was a source of significant profits in 2024, with our position sold in November generating 23% profit over an 8-month holding period.

We attribute the recent strength of the gold price to a combination of a response to the weaker dollar (with which it has a long inverse relationship) in January and mounting investor anxiety about the potential economic consequences of President Trump's plans to impose sweeping trade tariffs.

While the gold chart ends January displaying a solidly bullish tone, the probability of a failed price breakout is not small, which is why we are only prepared to risk a 2% loss on this trade. If Trump's trade rhetoric translates into significant actual tariffs, we expect the dollar to resume its ascent. That would have negative implications for gold.

The current risk/reward proposition offered by gold justifies the purchase of a position, with the potential upside being a multiple of the circa 2% we are prepared to risk. As we have commented previously, perhaps the most bullish factor in our thinking that the upside potential of gold may yet be considerable is the lack of interest from the retail sector. Previous important highs in the gold price have coincided with rampant speculation by retail investors. That is not the case currently, as the charts on the following page illustrate.





The implied retail allocations to both gold and gold mining stocks are at the lowest levels seen in years, while the price of gold has moved to all-time highs. It is noteworthy that the previous peak in gold interest by the retail sector occurred during the previous period of strength in gold prices in the years following the 2008 Financial Crisis. We believe that this disparity between price and interest in the retail sector must inevitably end. Either sustained strength by gold prices will eventually ignite retail interest or the current lack of enthusiasm is a harbinger of lower gold prices ahead. Historically, retail investors have a less-than-stellar ability to forecast market moves, causing us to believe that the path of least resistance will ultimately be higher gold prices.

The diminished investor interest in gold equities is further reflected by the Gold & Silver Index (XAU) chart on the following page.

## GOLD & SILVER INDEX (WEEKLY)



XAU has yet to reach its price high achieved last November when the major technical resistance represented by the previous high of 2022 served to reverse XAU's rally.

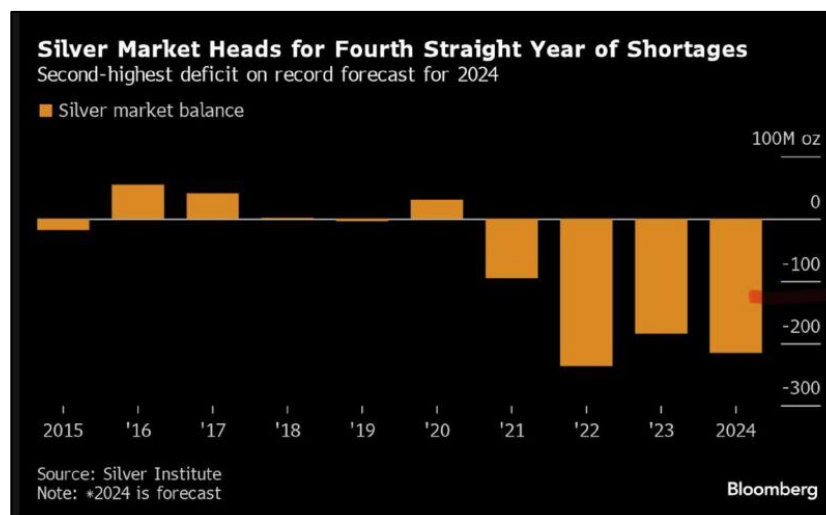
The very low level of current retail interest in gold will prompt us to purchase a half position in XAU should it trade above its 2022 price high. This is a departure for us, as we normally restrict our activities in precious metals to bullion, but the substantial upside leverage represented by the current lack of investor enthusiasm suggests to us that precious metals equities could rise dramatically should investor interest be captivated. As always, we would set a protective sell price a couple of percent below the purchase price to guard against a failed breakout.

## SILVER (WEEKLY)

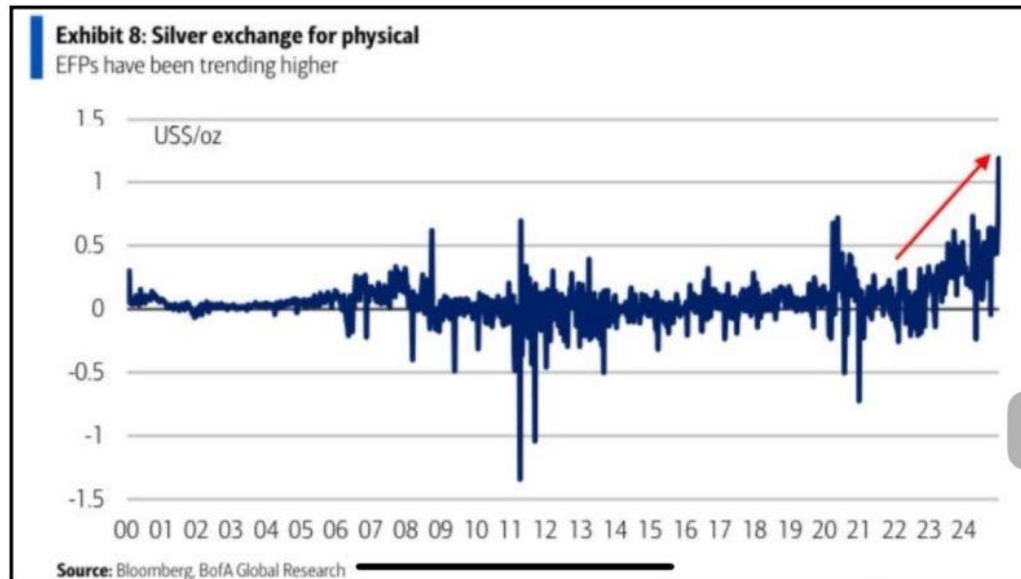


The silver market has been both intriguing to us for some time and frustrating in that it has yet to sustain a durable bull market despite compelling fundamental supply/demand considerations. The result has been that our forays into this market have produced meagre profits or small losses. Still, the silver market remains exceedingly interesting to us for its potential to ultimately produce significant profits.

The following charts, which we reprised from an earlier issue, will serve to demonstrate the source of our ongoing interest.



It illustrates that 2024 represents the fourth consecutive year of supply shortages for silver, which has served to deplete inventories significantly. The very high conductivity of silver lends itself to multiple industrial uses, with electronics and batteries being a major source of demand. It is expected that the supply deficit will continue for the foreseeable future. Unless the supply deficit is soon rectified, basic economics suggests that higher prices will eventually follow.



Another indication of the tightness of the silver market is depicted by the chart above, which demonstrates that holders of silver futures are currently demanding physical delivery at a higher rate than has been seen in decades. Such tight markets require only the right catalyst to trigger a sharp rise in prices.

The price chart of silver has a bullish tone (trading above both its 10 and 40-week moving averages). As it is our policy to wait until price action confirms our market view, we will only establish a new full position in silver on a breakout above the 2024 price high at circa \$35. In so doing, we would establish our initial protective sell price 2% below the 2024 price high to guard against a failed breakout.

If a new position is established and the protective sell price is triggered, we will establish a fresh position on a move to a new price high. As we believe the risk/reward potential for this market is unusually high, we are prepared to endure a series of small losses to participate in what we believe will eventually be a significantly higher move.

## ABOUT THE EDITOR

The Editor and Publisher of the Global Investment Letter is Jonathan Baird CFA. Prior to founding the Global Investment Letter, Jonathan spent more than 25 years as an award-winning money manager in Canada, most recently winning a Lipper Award in 2010 for managing the #1 Global Equity Fund in Canada. Jonathan managed several #1 ranked funds over the course of his career as a money manager, investing in all major industries, asset classes and markets. Along with his interest in the world of investment, Jonathan has been a lifelong student of history and uses the lessons of history to help interpret and provide context to current events. Jonathan no longer invests money for others, managing only his own account. The Global Investment Letter represents his personal thoughts and opinions.

Jonathan well understands the difficulty of the investment process and the essential role that quality information and opinion play in successful investing. Each monthly issue will contain comments on major markets, economics, geopolitics as well as investment ideas. There may also be a discussion of investment philosophy or practices and reviews of books deemed of potential interest to readers.

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