MH & ASSOCIATES • SECURITIES MANAGEMENT CORPORATION

INVESTMENT VIEWS

JUNE 30, 2023

MID YEAR OBSERVATIONS

Soft Landing Achieved?

Recent economic data have seemed to take a more positive bent, with the latest GDP numbers coming in stronger than expected. Employment has also held up well, with consumer spending holding in at a better than expected level. Other measures, including consumer confidence, credit conditions and durable goods orders, have shown some weakness as they have a more direct connection to higher interest rates.

We continue to take a measured approach to the current economic and financial environment. History shows us that there can be significant time lags between the Federal Reserve hiking interest rates and the negative tightening effects on the economy. That said, there are other forces, including government spending, demographics and various economic policies that seem to be working in favor of continued economic growth.

Bank Trouble Lurking

The banking scare earlier this year has faded from most investors' memory. However, it was just 3 months ago, in March, that Silvergate Bank had to be rescued by authorities and threatened to cause a systemic banking crisis. Though the memory of this event has faded, the risk of further trouble in the banking world is still with us.

As discussed above, the aggressive interest rate increases by the Federal Reserve have caused multiple problems in financial markets that have yet to be fully seen. Among the issues we are monitoring are problems related to unrealized bond losses, much tighter financial conditions for lower rated credits, and a rapid increase in interest rates for junk rated bonds, any of which might threaten an already uncertain economy.

Interest Rate Pause

The Federal Reserve will likely pause in their aggressive rate hike plan, as interest rates are now firmly above 5% and the latest inflation reading is below 5%. Many consider this position to be adequate to stifle inflation, returning it to the lower targeted rate of 2%. We remain skeptical that inflation can be controlled by interest rate policy in the long run, however a pause in hikes is certainly welcomed.

China Disappoints

Earlier this year China did away with their strict "zero COVID" policy and allowed the economy to begin reopening. Many, including us, expected a sustained period of significant growth as Chinese consumers released pent-up demand similar to what occurred here in the United States and industry sprang back to life. Instead, the reality is that economic growth in China is quite tepid so far and there has not been much in the way of government action to try and spur it. This weak growth is most clearly seen in various commodities from grains, industrial metals, oil and natural gas, all of which are significantly lower that last year. It is still our base case that the Chinese economy will continue to recover, albeit at a more modest rate.

Our Investment Style

As investors, we are dealing with unprecedented uncertainty. The financial landscape has change dramatically over the past 2 years, and warrants a higher degree of caution. At the same time, looking beyond the problems that threaten financial markets and the economy, we see many rewarding opportunities for investors. Our investment style - *making individual decisions about buying and selling each investment* - gives us confidence that we will be correctly positioned as the remainder of the year unfolds. We do not rely on a cheerful economy or outlook, but rather keep an close eye on the merit of each holding given the situation presented to us.

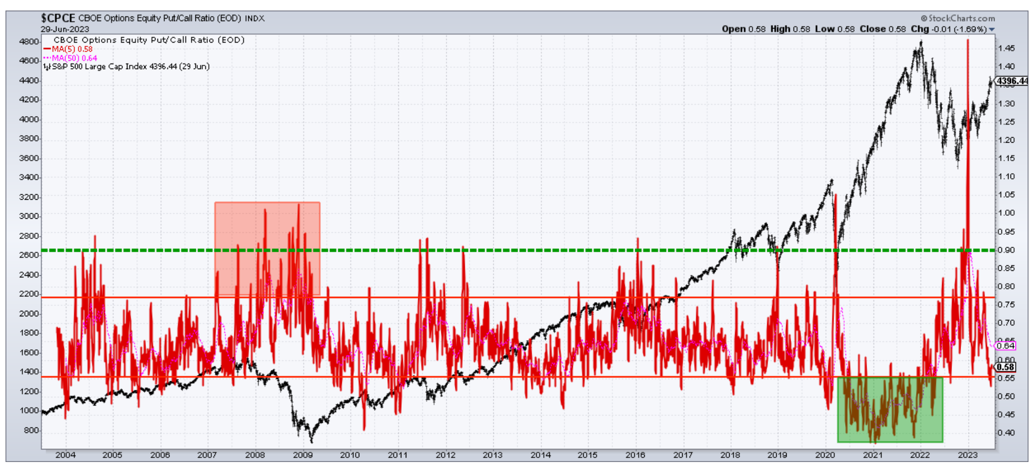
DOCTOR COPPER

Copper is often given the nickname "Doctor Copper" because the demand for the red metal is seen as a proxy for global economic health. Indeed, it has been a key commodity for the past several decades as demand from China and other emerging market nations have kept prices fairly healthy most of the time.

However, copper is taking on an even more important role in the global economy as major nations are seeking to shift to more electrified world. From obvious uses in electric vehicles, to less obvious uses in upgrading grid infrastructures, to wind turbines and solar panels, copper demand is set to explode over the next decade. At the same time, very few large copper deposits have been found in the past decade and virtually no new mines have been built to accommodate all this new demand. If a more electrified future is to be realized, copper demand will increase several fold from where it is now. Creating new supply is a lengthy process often taking 10 years from the time a copper discovery is made to when production at the new mine begins. Therefore, we anticipate that the price of copper will rise sharply to induce miners to search for and build new copper mines.

So far, our initial investment in this area has been disappointing as copper prices have been weak. As mentioned earlier in this newsletter, Chinese demand has been less than anticipated and US demand has been tepid with current economic uncertainty. In contrast, we also note the global stock of copper is near an all time low. We remain confident that the scenario we described above will play out, with copper prices likely to double as many industries scramble to lock in supply.

TECHNICALLY *Speaking*



In previous newsletters we have discussed the put/call ratio and how it relates to the markets. It provides a graphical depiction of how bullish or how bearish the options market is feeling. The chart shows in red the put/call ratio going back about 20 years. In general it has stayed within a banded area for this entire time. The periods when it moves beyond those bands tend to be when a trend change is coming and volatility is increasing. Extremely high readings (when more puts are being bought than calls) indicate an overly bearish feeling and can often indicate market bottoms as the sentiment is too negative. The opposite is also true when the options market shows more bullish sentiment (a low reading in the ratio). As you can see from the red shaded and green shaded areas, low reading can persist for some time. Generally there is not a huge spike down in the ratio, but spikes upward occur because fear is a much more powerful market emotion. Thrusts in the ratio above 0.9 (green line) tend to indicate that a bottom is forming, or likely already in as fear is overblown. Right now the ratio sits towards the historical bottom of the band and as we enter a seasonally bearish period of the year, the higher odds point to a softening in the market. However, this is not necessarily a reason to be concerned and several market indicators we track show that a continued move upward in the market is sustainable and barring any negative shocks (banks, interest rates, etc..), any correction should be relatively minor.

& Associates

MH & Associates Securities Management Corporation
2888 Loker Avenue East, Suite 318 • Carlsbad, CA 92010
23901 Calabasas Road, Suite 2005 • Calabasas, CA 91302
(626) 440-9694 • www.mhinvestments.net