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Sanctuary Corner

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Technology Tells This Market's Story – And It's An American Tale

Executive Summary

We remain positive on the equity market. We believe we are in a secular bull market that should last until nearly the end of this decade.

We believe Artificial Intelligence (AI), Blockchain, robotics, and Web 3.0 (crypto) will be the primary drivers of the U.S. economy and markets for the rest of the decade. Similar to how the widespread adoption of personal computers in the 1980s and early 1990s paved the way for the internet to revolutionize the global economy, markets, and social structures, we believe these emerging technologies will transform whole industries and redefine the way the world operates. This process has only just begun as we reach the middle year of this decade.

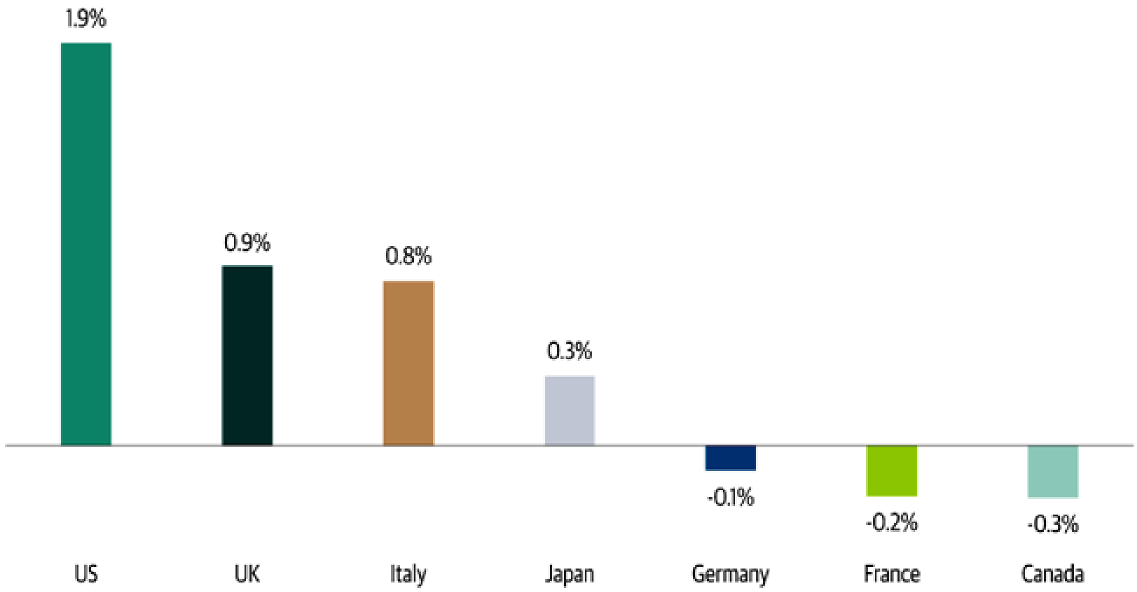
Our target for the S&P 500 in 2025 remains 7200–7400, and before the decade ends, we expect to see the S&P 500 reach 10,000–13,000. If we are correct, leaps in productivity should make for increases in Returns to Capital. Today the U.S. is already significantly above other countries in its level of productivity as the accompanying chart illustrates.

The risk to our outlook is if inflation begins to rise sustainably, causing the Federal Reserve (Fed) to switch course and raise interest rates.

Innovation Leads To Economic Dominance

The center of technological innovation and financial activity remains in the United States. President Donald Trump has made it clear his new Administration intends to keep it this way. We think this is positive for the performance of U.S. equities relative to stocks outside the country. If our view is correct , which we first highlighted in our Year Ahead report, we believe capital will be attracted to the U.S. – *and this has already begun.*

US Outpaces Other Developed Countries In Productivity Growth
Average Annualized Productivity Growth In Percent, 2020 Q2 – 2024 Q2



Source: Blackstone. "OECD, Macrobond as of 6/30/2024. Data for UK as of 3/31/2024. Data are annualized quarterly labor productivity measured as GDP, or output, per hours worked, and seasonally adjusted."

Trump's Policies And Rhetoric Draws Foreign Investment

President Trump has made clear that his economic policy is to cement American dominance in the forefront of innovation, technology, and finance, and to restore American manufacturing capacity and excellence. His motto is to "Make America Great Again." To this end, he has proposed using tariffs both to overcome foreign restrictions on American exports and to defend strategic industries. Investors around the world have taken note; some are already pledging to move capital to the U.S. because the U.S. has the best investment profile of any other country in the world, particularly on new technologies such as AI. Despite certain ongoing issues in the country, such as concerns over the deficit, the U.S. remains the center of innovation backed by the strongest economy in the developed world. Plus, the U.S. dollar continues to serve the world reserve currency – *and it is strengthening.*

Capital Already Coming To The U.S.

Japan's Softbank has committed to investing $100 billion in the U.S., while billionaire Hussain Sajwani of Dubai has pledged to invest $20 billion in new data centers here.

The New York Times

Japan's SoftBank Makes Big Investment Pledge Ahead of Trump's Inauguration. Again.

The technology company plans to invest $100 billion in U.S. projects, echoing the multibillion-dollar pledge it made after Donald J. Trump's first election victory in 2016.

By Maureen Farrell and Michael J. de la Merced

Published Dec. 16, 2024 Updated Dec. 20, 2024

CNBC

Trump announces $20 billion foreign investment to build new U.S. data centers

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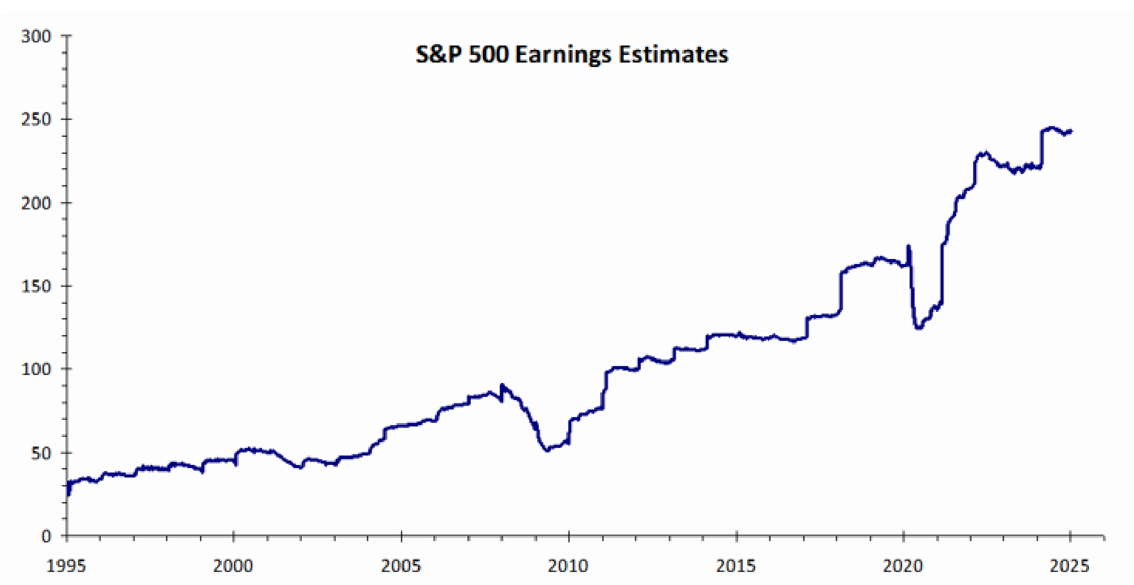
Growth in Productivity Should Boost Earnings

We expect growth in productivity, which should prove a boon to earnings and earnings growth. Wall Street strategists are estimating, on average, an earnings growth rate for the S&P 500 of 13%-15%.

S&P 500 Earnings Estimates Are Tracking Upward



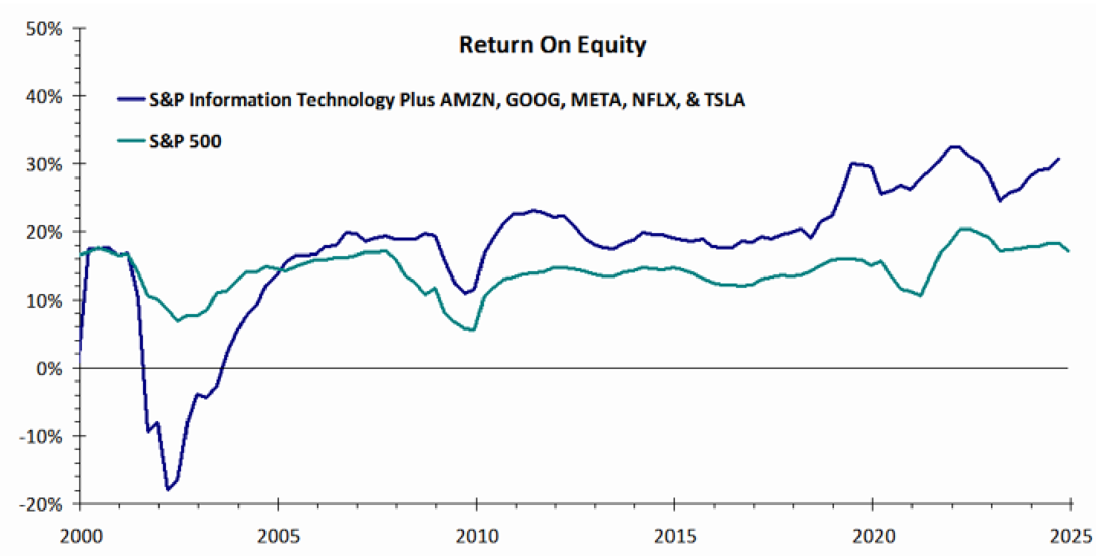
Source: Bloomberg, Sanctuary Wealth, January 11, 2025

Technology Retains Market Leadership

The Technology sector remains the leader in this market, in our view. While we expect hardware manufacturers and semiconductor companies to continue to perform well, we expect investors to shift their focus to software companies that create the applications that run on that hardware. This is the normal course of the technological cycle.

The return on equity (ROE) remains much higher for Technology and Tech-related companies at 30%, versus the overall equity market at 18%. This should continue to attract capital to the sector.

Technology Return On Equity Outpacing Broader Equity Market



Source: Bloomberg, Sanctuary Wealth, January 14, 2025

Manufacturing Coming Back To The U.S.

Taiwan Semiconductor (TSM) has built a chip plant in Arizona, and it is already manufacturing chips

TSMC's New Arizona Fabrication Plant Has Begun Producing World-Class Chips

tom's HARDWARE

TSMC's Arizona Fab 21 is already making 4nm chips — yield and quality reportedly on par with Taiwan fabs

News By Anton Shilov published January 11, 2025

It was alleged to be for AMD and Apple, but Raimondo did not say that.

A Review Of The Sectors Of The Market

This month we review the 11 sectors of the S&P 500 along with the performance of each sector relative to the S&P 500 index. When the relative line is rising, the sector is beating the index, when the line is falling the sector is underperforming.

SPDR Information Technology ETF (XLK) Is The Leadership In The Market
Technology (Top) With Relative To S&P 500 (Bottom)

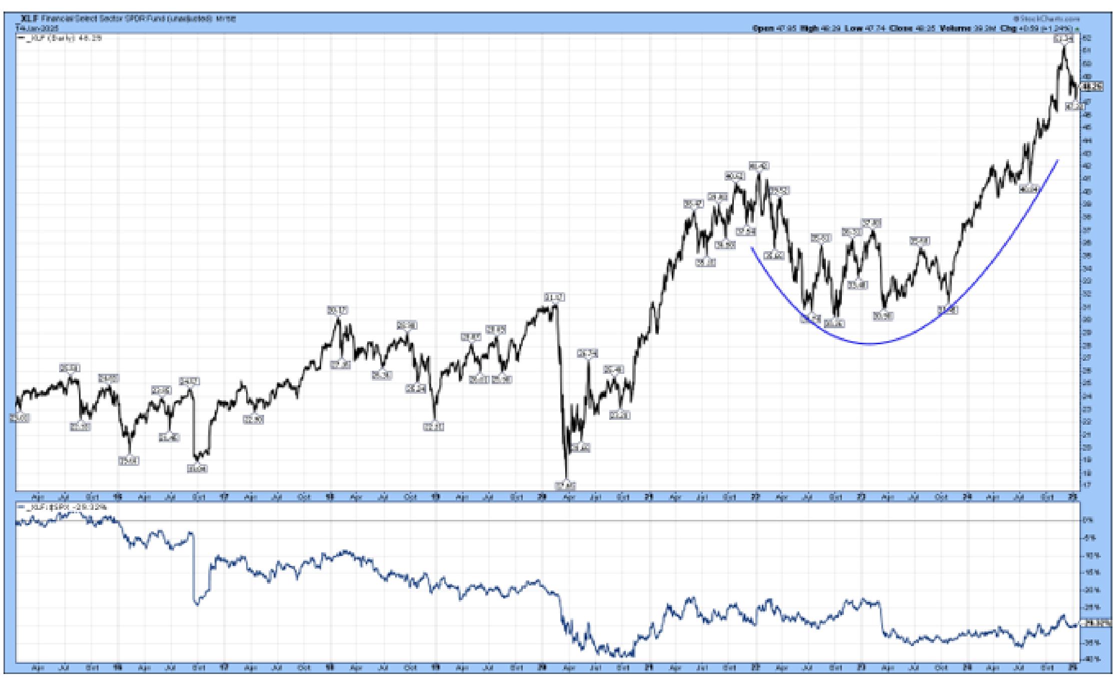
We Believe Software Is An Emerging Leadership In Technology
iShares Expanded Tech-Software ETF (IGV) (Top) With Relative To S&P 500 (Bottom)

VanEck Semiconductor ETF (SMH) (Top) With Relative Performance To S&P 500 (Bottom)

We Expect Financials To Do Well, Particularly The Banks And Capital Markets

The new Trump Administration is seen as friendly to the Financials sector and is expected to support a favorable regulatory framework for business. We have said that we also expect an acceleration for M&A and IPO activity. This should create an environment in which Financials should prosper.

SPDR Financials ETF (XLF) Improving With Banks & Capital Markets Favored S&P 500 Financials (Top) With S&P 500 Relative (Bottom)



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It Seems It Never Rains The Right Amount In Southern California

The tragic fires in Los Angeles have consumed lives and homes in the picturesque hills surrounding the chief city of the West Coast, but so far most of the region's critical manufacturing infrastructure has been spared. Economic losses will be felt, however, and insured losses will send shockwaves through the Property & Casualty (P&C) industry, which was already in decline a month ago. P&C stocks often decline after major disasters, then rally some months or quarters later when the remaining companies are able to raise insurance premiums after regulators decide they need those companies to survive and continue offering insurance. But we believe this pullback is not complete and could be a full bear market correction of 20% or more.

S&P 1500 Property & Casualty Index Declining, Risk Is More Downside

Consumer Discretionary Sector Should Do Well

Consumer Discretionary stocks include Amazon (AMZN) and Telsa (TSLA), both of which also have considerable exposure to Technology and innovation. While portions of the sector may underperform, we think these two companies could boost the sector as a whole.

SPDR Consumer Discretionary ETF With Relative Price Improving Significantly
S&P Consumer Discretionary (Top) With S&P 500 Relative (Bottom)

Communication Services Has Strong Strength

Communication Services includes companies such as Meta (META) and Alphabet (GOOG), which like Amazon and Tesla, have long tails in Technology. These companies represent immense computing platforms and back office capacity (cloud computing, data storage, communications) critical to the operation of the country and the economy.

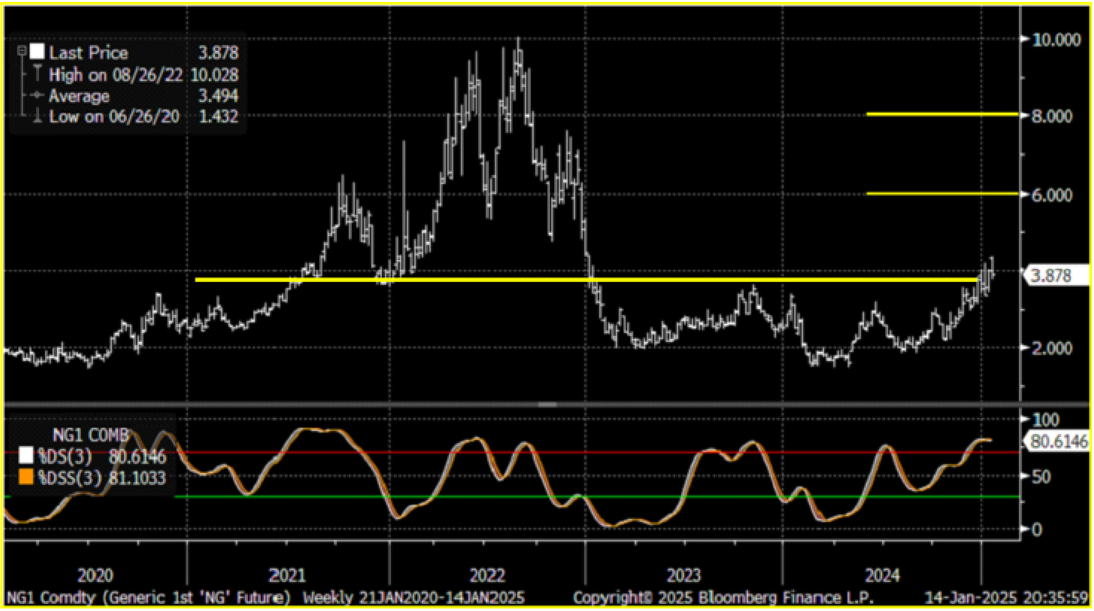
SPDR Communication Services ETF (XLC) A Leadership Sector
Communication Services (Top) With Relative To S&P 500 (Bottom)

Energy Stocks Represent Value

Energy stocks dominated the equity market in the early 1980s the way Technology stocks do today. Now Energy accounts for less than 3½% of S&P 500 capitalization. However, the policies of the new Trump Administration may provide an environment favorable to areas of this sector, and recently, natural gas prices have broken out of a two-year base. We think select Energy stocks, such as pipelines and gas, might provide an opportunity for investors, though we are not presently bullish on the entire sector.

SPDR Energy ETF (XLE) With Relative Price Weak
S&P Energy (Top) With Relative To The S&P 500 (Bottom)

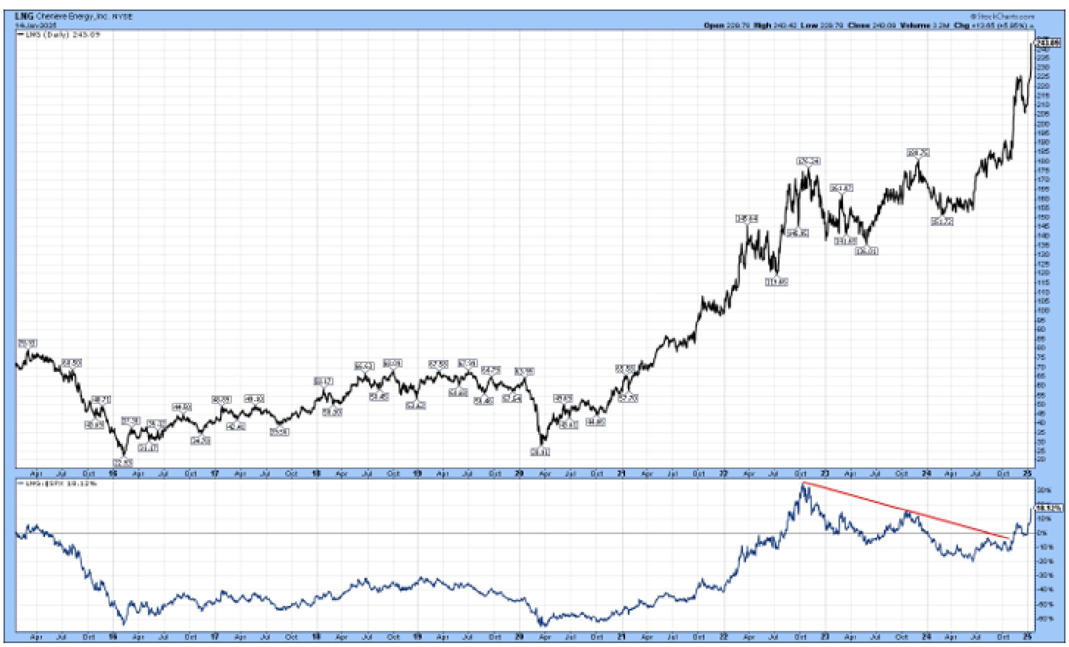
Natural Gas Price Broke A 2-Year Long Base: Target $6-$8 Dollars Per Million BTU



Tortoise North American Pipeline Fund ETF (TPYP) With 3.7% Yield (Top) Breaking Out Of Base With Improving Relative Price (Bottom)

Kinder Morgan (KMI) Is Rising From An 8-Year Long Base With 3.8% Yield (Top) With A Breakout In The Relative Price (Bottom)

Cheniere Energy (LNG) Price (Top) And Relative Price (Bottom) Both Rising Strongly

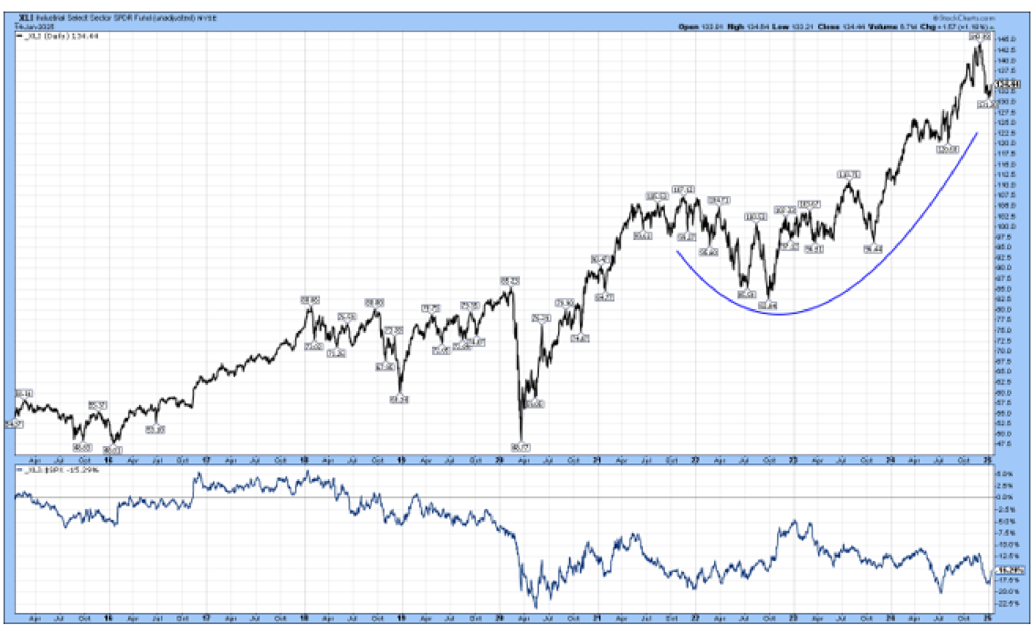


Pipelines Are Doing Well With High Yield
Alerian MLP ETF (AMLP) (Top) With Relative Price (Bottom) With 7% Yield

Select Industrials Can Do Well

We think re-shoring and near-shoring of manufacturing is likely to bode well for many companies in the Industrials sector. China has long sought to dominate global manufacturing. However, reciprocal tariff policies and widespread disapproval of China's increasingly aggressive and militaristic posture have created significant challenges for the country. Additionally, China's inability to drive domestic consumption, plus its financial struggles—exacerbated by over-indebtedness from its push for manufacturing dominance—have left the country vulnerable. Meanwhile, American firms are showing signs of recovery, bouncing back from years of seemingly unfair competition on the global stage. Smart tariff policies, while restricting some imports, and domestic spending can boost stocks in this sector.

SPDR Industrials ETF (XLI) (Top) Expected To Improve With Relative Also Improving (Bottom)



Materials Remain In A Bear Trend Except For Gold

China has been a major consumer of Basic Materials for much of the past 30 years, but as its economy grinds to a far slower pace, demand for materials has slowed as well.

Meanwhile, rebuilding after the Los Angeles wildfires may very well increase prices domestically in a number of Materials industries, such as lumber and copper; however, that movement may be as far out as a year. So, we expect Materials to remain an underperforming sector.

SPDR Materials ETF (XLB) (Top) With Relative Price (Bottom): A Weak Sector

Consumer Staples Likely To Remain An Underperforming Sector

The Consumer Staples sector is dominated by companies that are leveraged both to interest rates, which are rising, and to consumer sentiment and spending. While consumer sentiment seems to be improving, rising interest rates and demand for these products has fallen. This is also an expensive sector based on its low revenue and earnings growth rates.

SPDR Consumer Staples ETF (XLP) (Top) With And Relative Price (Bottom) Both Are Falling Sharply With A Bearish Outlook

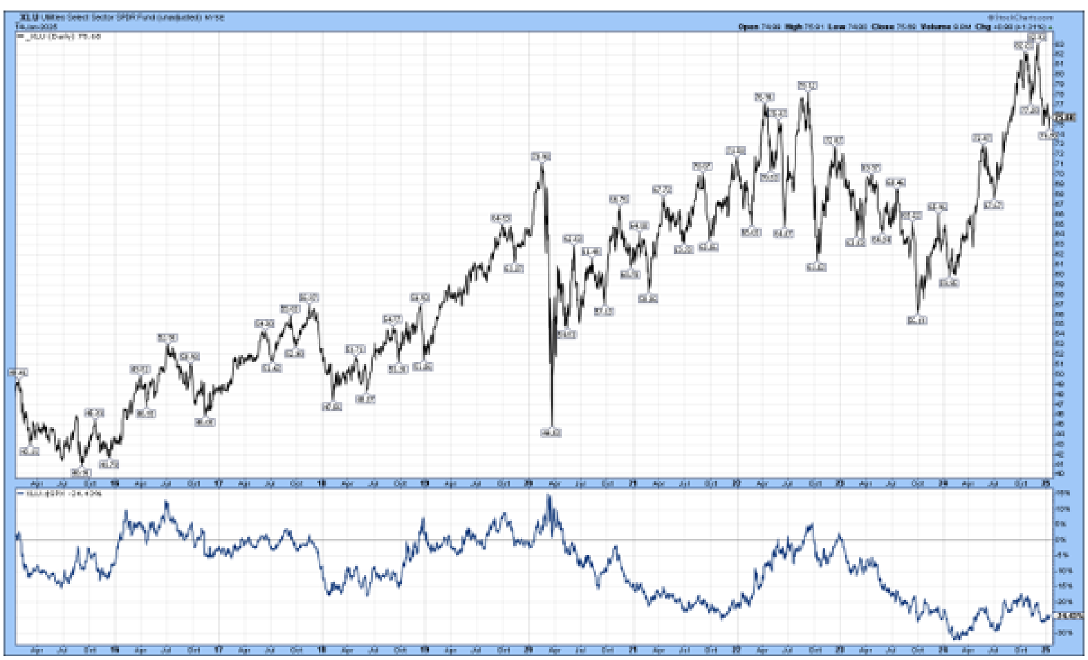
Higher Interest Rates Can Dampen Both Utilities and Real Estate

Utilities and Real Estate stocks generally require large investments of borrowed capital, making them vulnerable to swings in interest rates. As rates climb, these sectors will normally decline in relative performance.

Select Utilities stocks might do better in the current environment because of the tremendous increase in electricity demand, as driven by AI datacenters. These centers consume vast amounts of electric power, despite efforts by companies like Nvidia (NVDA) to introduce more energy-efficient chips.

SPDR Real Estate ETF (Top) With Relative Price (Bottom) With Both Underperforming

Utilities Performing Better With Demand Increasing For The First Time In 20 Years SPDR Utilities ETF (Top) With Relative Price (Bottom)



Health Care Stocks Are Extremely Weak With No Bottom In Sight

The Health Care sector feels like it is in the intensive care unit. The outgoing Biden Administration was seen as friendlier to Health Care than the Trump Administration. The stocks have been lagging for over two years with no bottom in sight. In our view, there will likely be increased pressure on profit margins for pharmaceutical companies and hospitals than in recent years as the government seeks to limit rising costs for consumers and mandated spending programs.

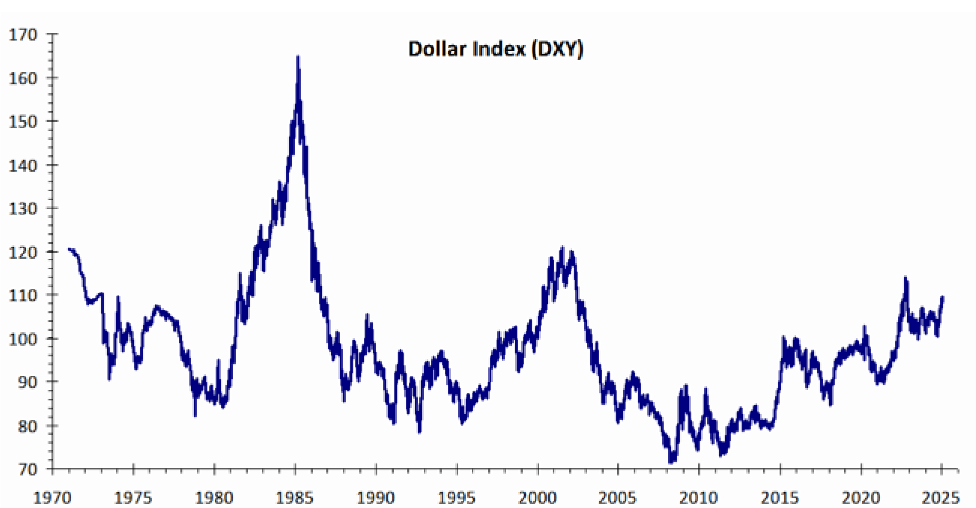
SPDR Health Care ETF (Top) With Relative Price (Bottom): Both In A Bear Trend

U.S. Dollar Rising

The U.S. dollar is rising against every major currency. Part of this is the interest rate differential between the dollar and other currencies; only the British pound has comparable interest rates at this time. Another reason is that the U.S. economy is the best of all the major world economies, and while it does have its problems, the U.S. has the nicest house on the global block of ugly economies.

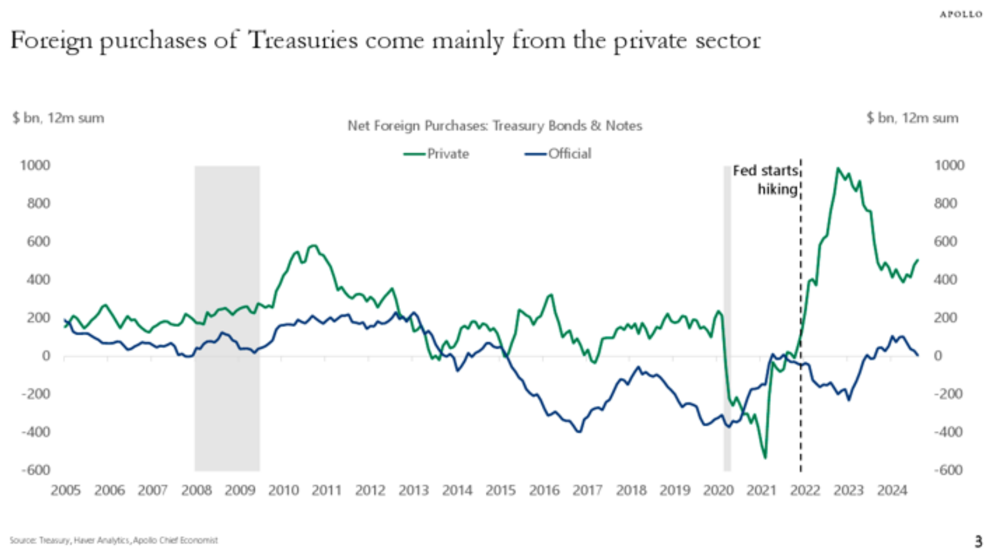
Still, another reason the U.S. dollar is rising is that the United States remains the top destination for investing in technology and innovation. It's where innovation happens, where ideas are developed, and where production takes place.

US Dollar Index (DXY) In Decade-Long Rise Reversing Major Downtrend



Source: Bloomberg, Sanctuary Wealth, January 11, 2025

The Demand For US Treasuries Remains Strong With Buying From The Private Sector



Source: Apollo Research, January 14, 2025

Rates Are Tricky Both The Bull & Bear Are Showing Up

With the Federal Reserve being data-dependent, market movements are heavily influenced by how reported data compares to expectations. This is causing volatility in the fixed income market. After the December Fed meeting's hawkish rate cut, rates rose and continued to rise on strong economic data. But the recent Producer Price Index (PPI) and Consumer Price Index (CPI) came in better than expected, and rates fell from their recent highs. We believe there will be continued volatility in the market with the Fed being so data-dependent. We expect a tight range that should not derail either the growth in the economy or the bull run in equities.

2-Year Treasury Yield Holds Resistance At 4.3%, A Break Of This Level Points To 4.6%

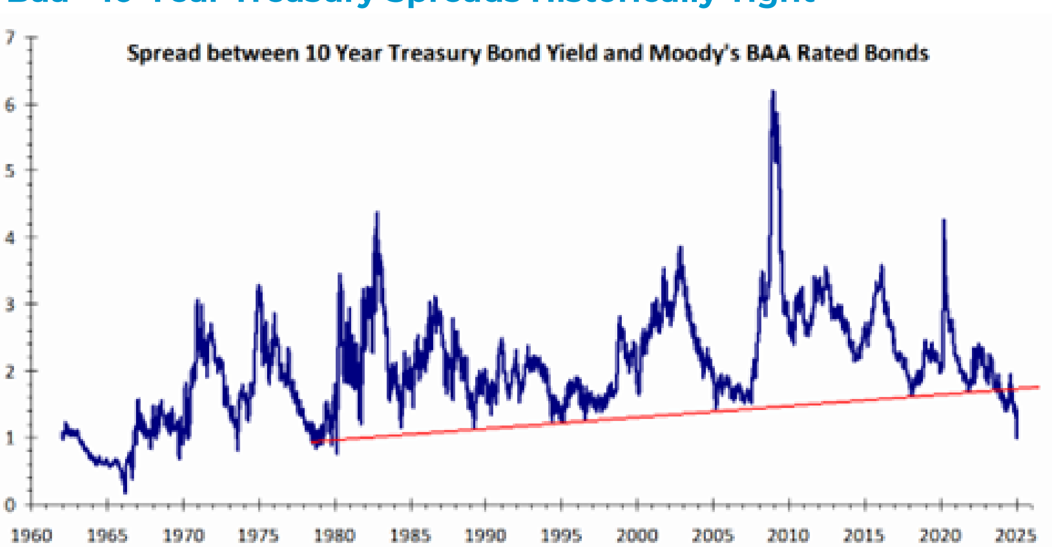
10-Year Treasury Yield Held At 4.7% But The Range For 2025 Seems 4%-5%

No Stress In The Market

The spread between Baa corporate bond yield and the 10-year Treasury yield is an important barometer of any potential stress that could be building in the financial system. If this were to occur, it would be a negative. But we have the opposite: spreads remain stable and are still falling (tightening). This is a bullish indicator for the equity market.

The high yield market and the leverage loan market are also trading strongly, which is confirmation of no stress in the market on this recent equity sell-off.

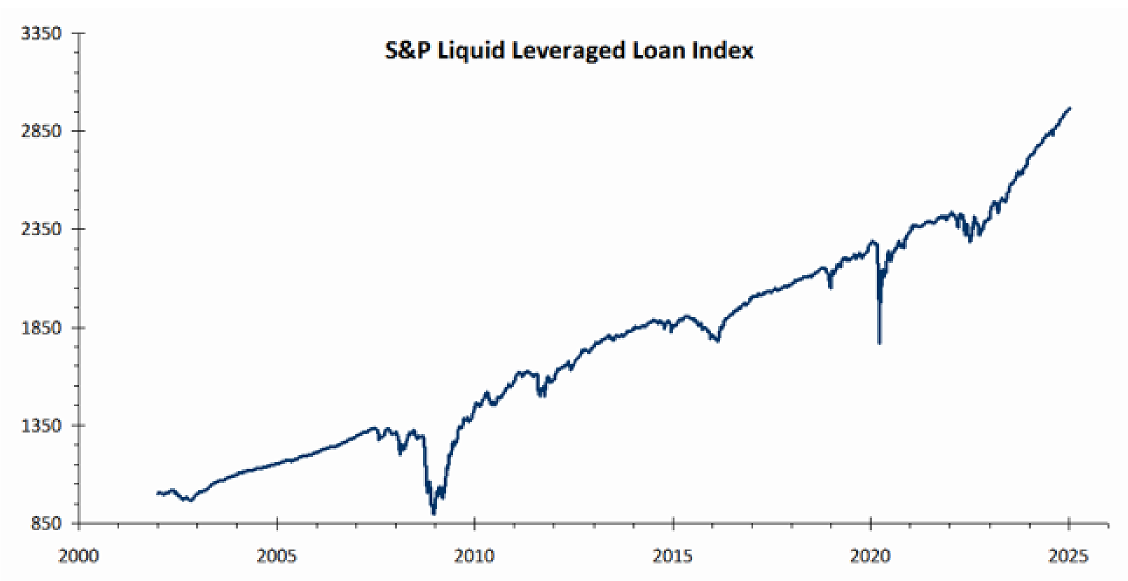
Baa - 10-Year Treasury Spreads Historically Tight



Source: Bloomberg, Sanctuary Wealth, January 11, 2025

iShares iBoxx High Yield Corporate Bond ETF (HYG) With Buy Signal 14-Day Stochastics

S&P Liquid Leveraged Loan Index Continuing To Move Higher



Source: Bloomberg, Sanctuary Wealth, January 11, 2025

iShares Flexible Income ETF (BINC) Should Improve With 6% Dividend Yield
14-Day Stochastic Appears To Be Bottoming

Gold Is Still Glittering
Small Positions In Gold Might Add Some Stability To Portfolio Values
Our Long-Term Target Is $4000

Bitcoin Is Likely To Continue To Advance Over The Long Run, In Our View
Near-Term Technicals Point To $113,000-$150,000 On A Breakout

DISCLAIMER: Comments regarding Cryptocurrencies or Cryptocurrency-based securities are for informational purposes only. No part of this communication should be construed as investment advice and is not to be considered a solicitation with respect to the purchase or sale of any Cryptocurrency-related product.

Last Words

Rising earnings expectations driven by productivity gains from Artificial Intelligence (AI) and other innovations are just beginning to show significant economic and efficiency improvements. In our view, this should lead to substantially higher returns on capital. We believe the advent of AI has set conditions for a secular bull market that will last the rest of the decade.

Risks to our outlook:

1. The Fed has to reverse course and raise interest rates because inflation returns.
2. Concerns over the deficit bring out the bond vigilantes, driving rates higher.
3. President Trump's policies are expected to negatively impact the economy, driving stocks lower.

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