January 10, 2024

Dear Valued Castleview Clients & Friends:

Looking back on the past year, real (adjusted for inflation) economic growth ended up weaker than many expected to start 2023. My view that it would continue to be difficult to “fight the Fed” proved accurate, but notably non-linear in a year of significant shifts in monetary policy. The Fed’s published Balance Sheet run-off (QT) and interest rate increases introduced a challenging policy injection not seen in recent years. The year began on a sluggish note facing such strong headwinds as rising rates also pressured bank balance sheets which contributed to notable bank sector weakness in the first quarter of the year.

In March, three of the largest bank failures in our nation’s history set the stage for expanded Fed involvement and opened the door for announced balance sheet reductions to be fully sterilized by RRO actions. Simultaneously, the launch of the Bank Term Funding Program (BTFP) enabled the offloading of specified collateral from bank balance sheets to the Fed on a temporary (1-year) basis without requiring the typical re-pricing of impaired asset values. In turn, the bellwether S&P 500 Index moved higher through Q2 before returning to early April price levels by late October as hopes of resurgent economic growth dissipated.

As we moved into November, U.S. Government interest rates began to drop and global equity prices rebounded sharply higher. Financial asset prices spiked once Fed Chairman Powell hinted that interest rate hikes were complete. The continued strong correlation between financial asset prices and global central bank policies (see Fig. 4) leads me to believe that the Fed’s upcoming decisions on whether to wrap-up or extend the BTFP facility, its Quantitative Tightening (QT) program and the direction of base interest rate levels will each materially impact the direction of global financial asset pricing in the coming year as well.

Exiting 2023, it may prove noteworthy to mention that S&P 500 earnings estimates for Q4 declined 7% from September 30th through December even as the Index jumped more than 11% during the same period. If corporate earnings are able to meet these weaker revised estimates for Q4, then S&P 500 Index earnings will end flat versus 2022. At this point, large-cap U.S. equities appear to be “all in” on the notion that further Fed involvement is forthcoming in 2024. Stagnant earnings coupled with higher equity index levels have led to S&P 500 Index valuations priced for near-perfection. Current Price-to-Sales ratios are at the highest levels of the past 25 years (excepting the two years of emergency fiscal and monetary stimulus measures enacted in 2020 and 2021). Even so, the SPX has risen in 20 of 24 election years since inception with another one presumably ahead.

	Dec 2023	YTD 2023
S&P 500 (broad equity market)	+ 4.54%	+ 26.29%
Nasdaq Comp (tech sector)	+ 5.58%	+ 44.64%
Russell 2000 (small caps)	+ 12.22%	+ 16.93%
Bbrg Barclays Agg Bond Index	+ 3.83%	+ 5.53%
Int’l Developed Market Stocks	+ 5.33%	+ 18.85%
Int’l Emerging Market Stocks	+ 3.95%	+ 10.27%
WTI Crude Oil	- 5.59%	- 3.79%
Gold	+ 1.14%	+ 12.82%

Pending further stimulus inputs and the possibility of a reacceleration of inflation pressures, we continue to see potential for an unusually wide range of outcomes in markets. U.S. large cap leadership (“Magnificent 7”) looks historically expensive while broad economic growth has been weak. Ongoing concerns surrounding geopolitical hotspots remain and we see nothing to indicate that continuing escalation will stop.

As a result, we believe a prudent response to current circumstances centers around a focus on one’s personal financial planning objectives. Specifically, reviewing asset allocations to affirm that risk of capital and loss of purchasing power are properly considered and balanced in portfolios. At the margin, we believe equity allocations should be reviewed and risk monitored where needed to better align with one’s specific risk profile. Unless this time is different, we are likely to experience a prolonged period of outperformance in Valuation-centric investing styles over the intermediate term. Of course, new data points continue to emerge. We commit to you that we will continue to monitor developments and keep you updated.

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Sudden Spate of Cyberattacks in Iran and Ukraine Coincide With Upcoming DoD Initiatives to Secure US *(by McAlinden Research)*

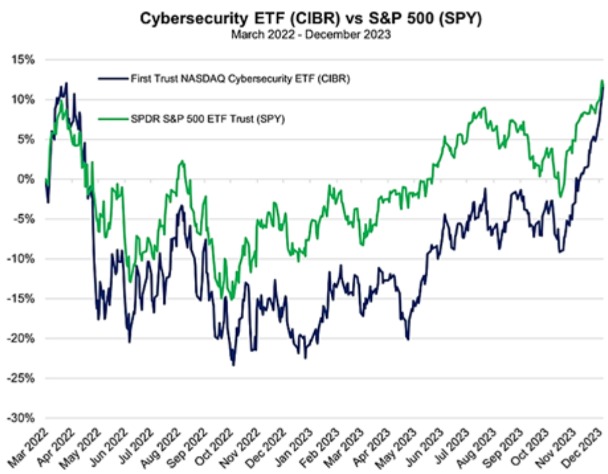
Services were disrupted late last month at up to 70% of Iran's gasoline stations, the result of an apparent cyberattack on a critical pillar of the country's energy infrastructure. Iran's Oil Minister Javad Owji confirmed Tehran's suspicion of a cyberattack, while Israeli hacker group Gonjeshke Darande (which translates to "predatory sparrow") took responsibility for the mass disabling of gas pumps. Unsurprisingly, the hackers stated that their targeting of Iran was a response to the aggression of the Islamic Republic and its proxies in the region. Per The Times of Israel, this is the second time Gonjeshke Darande claimed responsibility for a cyberattack that targeted Iran's fuel distribution system in 2022 and forced the Iranian state-owned Khuzestan Steel Co. to halt production after multiple systems were compromised.

This incident comes just a week after Ukraine's largest telecom operator, Kyivstar, was slammed by a sophisticated cyberattack of Russian origin that cut nearly 90% of its data connectivity. The scale of this outage is massive and, according to Reuters, the largest inflicted on Ukraine since the start of Russia's formal invasion of the Ukrainian mainland in February 2022. Kyivstar serves nearly 25 million mobile subscribers and more than 1 million home internet customers. The temporary shattering of Kyivstar's network kept many civilians from receiving alerts of potential Russian air assaults and disrupted the air raid alert systems in parts of Kyiv. Pro-Russia hacktivist group KillNet claimed responsibility for the attack but, the hackers posted no substantiating evidence.

Though the hacker collectives behind these attacks, as well as many others, are not typically formal military intelligence agencies, their objectives are interlinked with such organizations and there is usually more of a relationship than meets the eye. Microsoft's fourth annual Digital Defense Report, released in October, notes that state-backed cyber operations are broadly becoming more advanced and aggressive and are increasingly pairing campaigns to breach computer systems and spread government propaganda and coincides well with the pattern of recent spate of cyber warfare activity.

The US has not been immune to wide-reaching cyberattacks against critical infrastructure and government agencies. As covered in 2021, state-backed hackers were able to insert malicious code into an update of Orion, one of SolarWinds' platforms. It initially became clear that the Departments of Commerce, the Treasury, and State – which used SolarWinds' IT infrastructure – were breached at some level, but that was only the beginning. More than 18,000 SolarWinds private and public sector customers installed the malicious updates, including at least nine federal agencies were confirmed compromised. The SolarWinds breach had a significant financial impact on affected organizations, with the attack costing affected companies an average of 11% of annual revenue. That slice of revenue comes out to about $12 million per company. The SolarWinds spyware breach was disclosed to the public not long before a high-profile ransomware attack on Colonial Pipeline Co. that forced the shutdown of 5,500 miles of US pipeline carrying nearly half of all fuel supplies on the East Coast. This was only relieved after the pipeline firm paid a $5 million ransom.

The US's $886 billion National Defense Authorization Act (NDAA) for fiscal 2024, passed by congress and now awaiting a signature from President Biden, set out several new cybersecurity initiatives for the Department of Defense (DoD). Per CSO, these include the creation of a "cybersecurity risk inventory, assessment, and mitigation working group" and a cross-functional team to develop and oversee the implementation of a threat-driven cyber defense construct for the systems and networks that support the nuclear command, control, and communications mission. Interestingly, the NDAA will allow the US Army to access assets in the US civilian realm by conducting a pilot program to establish a Civilian Cybersecurity Reserve to provide the United States Cyber Command with human resources to effectively respond to malicious cyber activity and conduct cyberspace operations.



Gold and Bitcoin Break Out, Greenback Stagnant on Rising Expectations for Earlier Rate Cuts

(by McAlinden Research)

Spot gold prices recently surged to an all-time high north of $2,150. That capped a 16.5% rally since the start of 2023. At the same time, the unit price of the world's largest cryptocurrency, Bitcoin (BTC), tapped $42,000 for the first time in nearly 20 months – up more than 150% om 2023.

Though BTC has obviously risen more steeply than gold throughout the past year, due to its more volatile nature, their price appreciation has followed similar trajectories. Some have long posited that gold and Bitcoin could very well be complementary assets in some situations, sharing very similar monetary qualities and the potential to benefit from similar trends. Earlier this year, BlackRock CEO Larry Fink lent credence to the "digital gold" narrative, stating that Bitcoin is "digitalizing gold" and "could revolutionize finance". This was a massive stamp of legitimacy, considering BlackRock is the world's largest asset manager, responsible for $9 trillion AUM in Q1 2023. Fink went on to add that "Instead of investing in gold as a hedge against inflation, a hedge against the onerous problems of any one country, or the devaluation of your currency whatever country you're in – let's be clear, Bitcoin is an international asset, it's not based on any one currency and so it can represent an asset that people can play as an alternative." BlackRock is one of the asset managers currently in the running to launch the US's first spot-backed Bitcoin ETF.

One example of the Bitcoin-gold relationship played out earlier this year during the US banking panic that played out between March to May earlier this year – culminating in three of the four largest bank failures in US history. As trust was lost in banks throughout that period, investors apparently poured assets into Bitcoin and Gold to store their value and keep it remote from the next potential bank collapse. These commodities' values shift constantly in Dollar terms, but both are always fungible – one unit of either Bitcoin or Gold is always equal to another unit of the asset. If investors take custody of their gold or BTC, they can eliminate the counterparty risk that a bank may pose since Bitcoin is always stored on an immutable blockchain ledger and physical gold can be stored securely as well.

Ownership of Bitcoin is does not take the form of an IOU like a bank account, it is a cryptographically-secured bearer asset that can be stored in any amount at little to no marginal cost. It can be sent anywhere on the network across the world at any time with full settlement in minutes. Portability and infinitely scalable storage is one advantage that Bitcoin carries over gold, as the costs to securely move or store BTC does not increase based on the amount of the asset that is being transferred. Essentially, because Bitcoin has no mass, one BTC or one million BTC can be moved with identical speed and security, and at the same low cost. Obviously, storing or transferring one million ounces of gold (equivalent to 62,500 pounds of mass) relative to one ounce would incur much greater costs and risks. Another key difference relates to the nature of scarcity: The gold miner's resource is relatively scarce, whereas the Bitcoin miner's resource is

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absolutely scarce. Though there is some feasible limit to how much gold there is in the world, nobody knows where that limit actually is, given each individual's necklace or gold stash can't be accounted for and new, previously unknown deposits are discovered semi-regularly.

In June 2022, for instance, Reuters reported about 31 million tons of gold ore were newly discovered in Uganda with up to 320,158 tons of refined gold being extractable. That is a significant development for the long-term supply of gold, considering this discovery alone could potentially yield 53.3% more gold than all of the gold mined throughout history, which the World Gold Council pegged at 208,874 tons. Again, that is only an estimate and nobody can feasibly calculate how much gold has actually been produced and is in circulating supply. This is not the case with Bitcoin. Not only can it be known with absolute certainty that there will only ever be 21 million BTC mined, but it can also be easily verified that as of 12:30pm UTC on December 4, 2023, there were exactly 19,560,881 BTC in circulating supply.

The difference in relative and absolute scarcity also plays out in how much new supply of each resource is produced. The primary driver of gold output will be the market price. Simply put, when gold prices rise, gold miners will typically accelerate the production of gold to sell more at a higher price. The issue for miners is that the introduction of greater supply at an accelerated pace will likely be one of the factors that ends up extinguishing the higher prices that were created by strong demand conditions. This same scenario could be projected onto the producers of copper, wheat, oil, and many other commodities. The issuance of Bitcoin on the other hand, is programmatic and not controlled by any suppliers. Rather, it is controlled by a network protocol and mathematics that dictate an immutable schedule of distribution.

The similar trajectory that Bitcoin and gold have followed recently is largely related to shifting monetary policy at the Federal Reserve and its impact on the US Dollar (USD), which traditionally correlates inversely with both of the commodities. In particular, the Fed's series of rate hikes that have sent the upper limit of the benchmark Fed Funds rate to its highest level in over two decades appears to have come to an end. In fact, CME's FedWatch suggests that rate cuts are now being priced in by futures traders as soon as March. According to FedWatch data, there is now a 59.8% probability that at least one rate cut will trim 25bps from the benchmark overnight rate by March. A halting, or even a reversal, of the hikes that have helped the Fed tighten monetary policy in the US would have a significant impact on USD's value relative to other currencies. When interest rates rise in the US, the higher yields can attract investment capital from investors abroad who exchange assets in non-USD currencies for Dollar-denominated investments. This demand, in turn, raises the value of the Dollar compared to other currencies. In a similar way, if rates are to hold steady or even begin to fall, that can cut the appeal of the Dollar.

All the way back to August 2022, the US Dollar was seen as likely on the verge of a downturn, as the Fed was rapidly approaching what we termed "peak hawkishness"; the point at which rate hikes reached their maximum size and frequency. We wagered, from that point on, the central bank's rate hike regime would gradually reduce the size of rate hikes from 75bps at their largest to 50bps and then, eventually, just 25bps. Further, these hikes would become less frequent until they ceased altogether – likely the state of affairs we have now reached with just one hike in the past four FOMC meetings. The US Dollar Index (DXY) hit a more than 20-year high north of 114.0 that September, prior to retreating. Though the Dollar did rebound from lows under 100.00 earlier this year, it has not gotten anywhere near its 2022 high with recent prices near 103.5.

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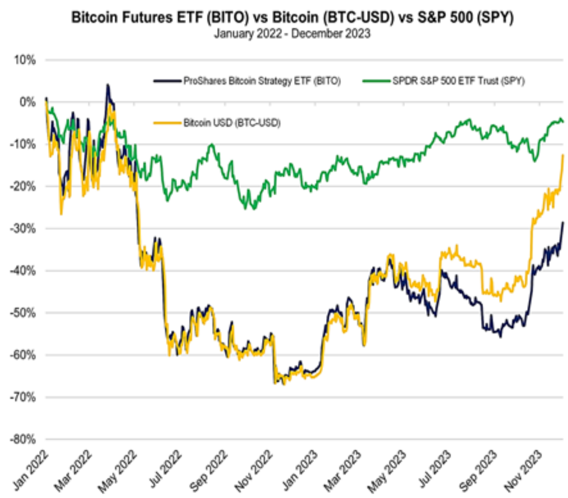


Weekly Crypto Wrap **Dec 22, 2023**

(by McAlinden Research)

As 2023 winds down, the total market capitalization of cryptocurrencies is very close to a yearly high at $1.66 trillion. Bitcoin (BTC), the largest cryptocurrency by market cap, is also very near its annual high, with its unit price trading near $43,700 on Friday morning. In the year-to-date period, that represents a 163.3% return – on pace to be the strongest year for BTC since 2020. December is currently on track to mark a fourth straight green month for Bitcoin prices. If BTC does close higher this month, it would be the first instance of such a sustained run in nearly three years.

A lot of the resilience in digital assets over the last couple of weeks has come from so-called “alt-coins”, the swath of tokens and coins that typically follow in Bitcoin’s wake. Bitcoin composes more than half of the entire crypto market, but its dominance has been whittled down slightly from just under 54.0% in early December to 51.5% in recent days, suggesting BTC has been outperformed by its competitors for most of the month. Throughout the past week, top 10 cryptocurrencies Avalanche (AVAX) and Solana (SOL) have reached 16-month and 19-month highs relative to BTC.

Bitcoin may be getting held up on the remaining uncertainty regarding an upcoming decision from the SEC on spot-backed BTC ETFs. Though news on this front would appear to be positive, detailing an increasing frequency of meetings between asset manager applicants and commission officials, recent price movement has not been reflective of increased optimism. This may also suggest that the immediate impact of a spot BTC ETF approval is already widely expected and priced into the market.

Numerous amendments to S-1 documents have been filed by BlackRock, ARK Investment Management, Bitwise, and other Bitcoin ETF hopefuls throughout the past month, suggesting that dialogue with the SEC has continued steadily in the wake of the regulator’s upset defeat in the DC Court of Appeals last August. As noted at the time, three Federal judges on the case, filed by Grayscale Investments, unanimously agreed with Grayscale’s assertion that SEC’s rationale for rejecting their request to convert its Grayscale Bitcoin Trust (GBTC) product into an ETF was “arbitrary and capricious”, exhibiting “unlike regulatory treatment of like products”, in reference to futures-backed Bitcoin ETFs that had been previously approved by the SEC. First in line for a final decision date will be ARK’s application in partnership with 21Shares, slated to be approved or rejected ***by January 10, 2024***. Though that is only the final decision deadline for ARK, a potential SEC approval could be handed down to all outstanding applicants on the same date to avoid giving any asset manager a specific advantage over others.

The January date has been highlighted as the most likely timeframe for an approval since August and there are potential implications for Bitcoin’s circulating supply, which remains relatively illiquid. Over 70.0% of BTC’s circulating supply has now sat untransacted for at least a year – a near record high.

We’ve previously gauged the impact of illiquid supply on market prices by utilizing market depth. Per Kaiko Research, it would have taken over 1,400 BTC to move Bitcoin’s price by 1% in January but, by mid-November, just 752 BTC was required to achieve a 1% price movement. With a dozen asset managers waiting for a green light from the SEC to begin accumulating BTC as backing for shares of their potential ETFs, a wave of demand could sweep over the market and carry significant ramifications for Bitcoin volatility.

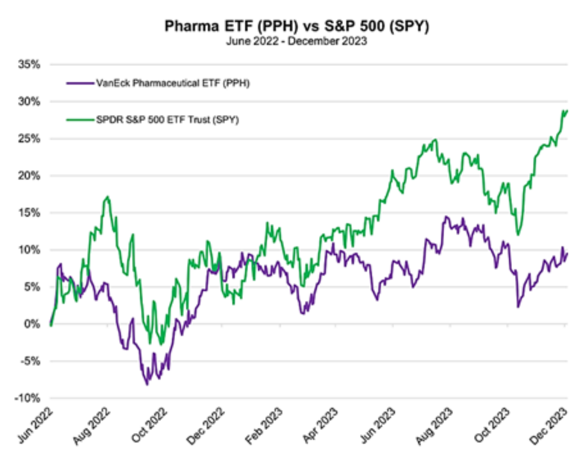
Big Pharma Consolidates Its Hold on Financing for Desperate Biotech Sector, M&A to Gain Steam in 2024 *(by McAlinden Research)*

Following a final nod of approval from the US Federal Trade Commission (FTC) last month, Pfizer has closed its massive $43 billion acquisition of Seagen – sealing the largest biopharma deal in almost four years' time. Though there was some uncertainty regarding the FTC's reaction to this deal, MRP noted in September that it was unlikely the commission would stand in Pfizer's way, following the sudden settlement of a previously-filed suit targeting Amgen's proposed $27.8 billion purchase of Horizon Therapeutics. That was the richest biopharma deal of 2022 and MRP posited that an ongoing wave of M&A activity among pharmaceutical and biotechnology firms would be bolstered by the conclusion of the FTC's legal action.

The closure of these two monumental deals, as well as several other factors, may set the stage for an this trend to gain further steam in 2024. A new PwC report notes that 2023 has been "a reasonably strong year" for deal value and volume in the pharmaceutical and life sciences sector. Moreover, they suggest 2024 will yield similar M&A activity across the pharmaceutical and life sciences sector, with deals reaching a "healthy" range of $225 billion to $275 billion. We originally posited that M&A activity would pick up among big pharma buyers and increasingly distressed biotech startups way back in the summer of 2022. Not only have cash balances been strong across the pharmaceutical industry throughout the past couple of years, but valuations of many publicly traded and privately held enterprises have been suppressed by a broader downturn in equity valuations since the start of 2022. In early 2023, more than 300 public companies were facing financing problems and a need to raise fresh funds within the next 18 months, according to investment bank Torreya Partners.

A souring IPO market throughout the 2022-2023 period pushed that option off the table for many privately-held biotech startups in need of funds. Moreover, Bloomberg has reported that venture capital (VC) funding for rising biopharma firms was slammed by rising interest rates and narrowing returns in 2022, slumping by -19%. With that oxygen being sucked out of the room, some have suggested that healthcare companies that might have previously resisted giving up some equity and control over their products to larger pharmaceutical firms may feel more inclined to make those partnerships to stay afloat now. Per a recent survey commissioned by CRO Icon, 48% of biotechs are now using partnerships with big pharma firms as a financing method. Further, VC funds are expected to total just $24 billion for the year—the lowest in four years, according to PitchBook.

According to an RBC count, the cumulative value of biopharma deals in 2023 tallied $128 billion, more than doubling up on $61 billion in deals in 2022. Furthermore, large-cap biopharma companies will retain $199 billion in cash at year end.



IDEAS TO CONSIDER

Similar to comments expressed over the past few quarters, and our expectation for continued uncertainty and volatility in financial markets in 2024, we continue to recommend to clients of the firm stay diversified and scrutinize your long-term financial planning objectives. It is these planning objectives formulated in close consultation with the expertise of your advisor that should largely dictate macro-level asset allocation decisions.

Our current outlook continues to recognize the need for investors to defend against both rising prices and higher than average valuations in large cap US equities. To defend against rising prices, an increased allocation to commodities may prove beneficial as they did in 2020-2021. Furthermore, the Fed has indicated that interest rate hikes are finished, and if so, U.S. interest rates should be flat to lower in the coming year.

Finally, as we look ahead, and as personal circumstances dictate, it may be worth considering a greater tilt toward value-oriented and international (DM and EM) equities, high-quality intermediate duration fixed income, as well as an increased allocation to what are often times referred to as “alternative investments” (commodities, tactical and/or hedged equity strategies as well as selective private credit or equity strategies). Monitoring balance sheet strength remains a focus in 2024.

In closing, on behalf of the entire Castleview team, thank you for your continued trust and confidence.

Sincerely,

Scott

M. Scott Zachary
Director – Investment Management

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