CAPITAL INVESTMENT COUNSEL

The Columns

February 2023

It's hard to tell who's having a tougher February: stock investors or weather forecasters. In Raleigh, we went from 45 degrees with driving rain to 80 and sunny in four days. With three seasons in a week, it's impossible to figure out what to wear. Stocks are the same. The S&P rode into February sporting an 8% year-to-date gain. From Valentine's Day through month end, that gain dwindled to only 4.5%. Last month's Column's read like a love letter to the NASDAQ. True to form, it's still leading the charge but even the good ole NASDAQ 100 has seen its gains cut from 16% to 11%.

I pay attention to the market's performance but more importantly to what groups are driving that performance. Looking under the hood, I still like what I'm currently seeing. Three of last year's winners were oil, utilities, and consumer staples (think basics like toilet paper and toothpaste). As the economy slowed last year, investors piled into those three groups, but 2023 has been a different story, at least so far. Oil is only up 2%, utilities are down 4%, and consumer staples are down 2%. Investors are waking up to an economy that's resilient and strong. The Federal Reserve appears to be doing everything possible to choke off growth, but the consumer is staying strong.

The underperformance in those three groups may be a result of money flowing back into growth. I feel tech is the best way to participate in the modern economy. In the past, you bought the old school cyclicals like Caterpillar or Dupont. Those two are still solid investments, but I like the global reach of semiconductors or the social media giants like Meta and Google. Semi's have currently popped to a 19% gain this year and the social media subgroup is up 12%. Look around your house and notice that everything seems to have a semiconductor chip. Try getting through the day without a Google interaction and let me know how that goes. I finally gave up and went full Google in my personal life: phone, cell service, and Google fiber internet ha-ha.

We're seeing a wide diversity of investor opinions. You have those who are simply unsure, and I understand that. There's a lot of unknowns out there from the employment numbers, housing sales or rising interest rates -- take your pick. Others see a light at the end of the tunnel and think it's a positive. They see the economy as improving and stocks should lead the way. I'm in that camp. Finally, you have the doom and gloomers. They feel things have never been worse and that stocks are ripe to make fresh lows below 3000 on the S&P. Remember the S&P currently sits at 4000 so that means a 25% drop from our current level.

I'm not persuaded by their logic. That's not the way markets have worked during my 37 years. Yes, bad things can happen to stocks, but that may have already happened last October, when the S&P was down 25%. Sell-offs of that size are rare and typically mean the end of the downside as opposed to the beginning of more selling. We've only seen it ten times, but after the market had a 25% intra-year selloff, stocks were higher nine times out of ten a year later with an average gain of 38% a year later. *(Source: Ryan Detrick at Carson)*

The 200-day moving average is the indicator that shows if a stock is in a long-term upward or downward trend. Most stocks were well below their 200-day average when the market bottomed out last October. Investors were seemingly selling everything in sight. That doesn't often end well for the sellers. Fast forward to late January and almost 70% of the S&P 500 had recovered back over their 200-day average to show the market in potential rally mode.

We've seen it happen seven out of seven over the last 23 years, and that type of recovery has meant the worst was over. *(Source: Urban Carmel)* Sure, stocks are not going up in a straight line, as they demonstrated last week, but I feel the direction is higher. By the way, if the 38% recovery holds true, that would put the S&P at 4800 in mid-October. From our current level, that's a potential 20% move you likely wouldn't want to miss. If you have any comments, feel free to contact me at heddins@capital-invest.com or call me at 919-656-0836.

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