CAPITAL INVESTMENT COUNSEL

The Columns

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I used to have great memories of Jackson Hole, Wyoming. I skied there during spring break and fell in love with the beauty of the Tetons. Unfortunately, Fed Chair Jerome Powell has diminished my love for Jackson Hole over the last two years. The Federal Reserve holds their annual symposium in Jackson in late August. For most of my career, it's been a non-event for markets but that changed last year. At the 2022 summit, Powell started his war on inflation and declared he would vigorously bring down consumer prices by any means necessary. Markets didn't like it and the S&P dropped 12% from August 26 through October 12, 2022.

The market's nosedive last year spooked investors as to what Powell would say in 2023. It appears many of them got a head start on selling. The S&P is down 3.5% so far in August as interest rates pushed to levels last seen in 2007. The good news so far is that like the big bad wolf, Powell huffed and puffed in Jackson Hole late last week, but he doesn't seem to plan on blowing the markets' house down in 2023.

Here's some thoughts on August selloffs and rising rates. I get it, the market was probably (long) overdue for a pullback. Selloffs are never fun, but they're typically part of the process. Ryan Detrick at Carson notes that whenever the market was up 17% plus going into the 8th month, August was positive only 27% of the time and declined 1% on average--not the best odds.

Rates just hit a 10 year high on the benchmark US Treasury. What's your reaction? Fight or flight? Simply yawn and move on? Maybe excitement? I'll choose excitement and stick with my 2021 mantra that interest rates are going higher because things are getting better. Jason Goepfert at Sentiment Trader agrees and has the stats to back it up.
Goepfert's database shows that this has happened seven times before. Stocks were higher six months later all seven times with an average gain of 4.3%. One interesting twist is that markets were higher a week later only 57% of the time indicating another small selloff may be lurking this week. In addition to the positive six-month trend, markets were higher a year later 71% of the time with an average gain of 11%. With that potential longer-term tailwind at our back, I'm inclined to take advantage of any selloff and buy a few of my favorite stocks.

I'm getting a little weary of waiting for China's turnaround. Sure, they've botched their COVID reopening this year and growth is down from where it should be, but that appears to be reflected in Chinese stock valuations. Baidu and Alibaba are two great examples. In January 2021, Baidu traded at 30 times earnings and Baba was at 29 times. Fast forward to 2023 and we see Baidu at 14 times next year's earnings estimate and Baba at 10 times. On top of that attractive PE ratio, Baba just recorded one of their top revenue growth years -ever. It reminds me of META stock last spring before their turnaround. High growth companies selling at a deep discount.

I don't think we need a lot to go right for these stocks to move higher given how negative the current sentiment seems to be. The match that lights the Chinese market's turnaround may be the September 1st cover of The Economist. The cover shows Chairman Xi riding a hybrid of a dragon and a snail and says, "Xi's Failing Model". I like that the news flow out of China isn't pretty, but the stocks are hanging in well above the lows from last year. To my mind, most investors who wanted to sell their Chinese stocks have already done so. We'll see what happens.

Let's close with another positive--profits on the S&P rocketed to nearly 12% this quarter. That's the highest in over a year and sits 23% above the average. It feels like the market is taking note and may be another reason stocks continue to climb. Thanks to Charlie Biello for the stat. If you have any comments, feel free to contact me at heddins@capital-invest.com or call me at 919-656-0836.