CAPITAL INVESTMENT COUNSEL

The Columns

June 2023

I've had a busy spring of speaking engagements and I like to finish my talk with two things: a highlight reel and a question. Let's look at the high light reel before moving on to my question. Here's 2023's list of things going right:

Unemployment is near record lows.

Inflation has been cut in half over the last 9 months.

The American consumer remains seemingly strong and in the mood to spend.

Housing, the bedrock of the economy, is solid in the face of rising rates.

After looking at that laundry list of positives, I'll ask my question – what are you waiting for? What further good news is it going to take to convince you to buy?

I've had this conversation countless times and the consensus answer is "I'm waiting for the recession." What recession is that and why do you think we'll have one is my response. In my experience, a recession is when a plane loses all four engines and can no longer fly. It's not typically one single thing that takes the economy down, it usually takes a combination of factors. As long as a plane has at least one functioning engine, it can keep flying. By law, planes are required to be able to fly for 5 hours on one working engine. I think our economy is much stronger than that. Looking at my highlight reel, our economy seems to have all engines in good shape.

I love that most investors don't seem to believe this and that's not just anecdotal evidence. As of May 19, 2023, investors were sitting on $7 trillion in money markets. *(Source: Goldman Sachs)* Sure, money markets are more attractive now that they're yielding 4.2% but the irony is that since that May peak in cash, stocks responded with an impressive rally: the NASDAQ 100 moved 8% and the S&P responded with a 3.5% gain. I like the large number of market doubters because 2023 has started strong *without their help*. If the haters begin to buy, that could help fuel a strong 2nd half of the year.

The fact that we're in June may mean this rally has staying power. I love June for many reasons. Long nights and warm days without excessive humidity. But most of all, I love that the June's market low is typically equal to or greater than the market's close in May. *(Source: S&P)* This run has been intact for 52 years and I'm hoping to continue the run in 2023. The S&P has already logged a 4% gain month-to-date so it will take a nasty selloff to take those gains back.

Gaze back through the best performing stocks of the last few years and you'll notice a common theme. Most of the big winners were the big losers of the year before. In early 2020, it looked like everyone hated the energy stocks. Oil stocks responded with an 80% rally over the next 8 months.

In 2022, it was big cap tech's turn to be shunned. QQQ answered with a 41% rally from October 2022 through last week. So, who is currently hated? It seems to be the regional bank stocks. Even after a 13% rally, the regionals are down 27% so far this year. The small caps were also on the "do not touch" list until two weeks ago. Small caps had languished with a paltry 2% gain through early May. Someone got the memo and small caps, as of this writing, have rallied 10%.

With a 10 percent weighting, small banks make up a large portion of the Russell Small Cap Index so further strength in the Russell may pave the way for more recovery in the regionals. I've long felt 2023 was similar to 2011. Like this year, 2011 had a debt ceiling crisis.

The market bottomed in October 2011 and finished the year with a 14% rally. It tacked on another 16% gain the following year to bring the total gain to 30%. Regional banks liked the action as well and notched a 51% gain from October 2011 through year-end 2012. Maybe this time will be different, but 2011 could be the playbook to use for how things may play out. Let's close it out with some positive vibes from Ryan Detrick over at Carson. The S&P closed out the 1st quarter with a gain greater than 5%. That makes two quarters in a row in the plus 5% column. That's happened 23 times over the last 73 years. The market was higher a year later, 20 out of 23 times with an average gain of 13%. That high light reel keeps telling us things are better than you may think. 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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