CAPITAL INVESTMENT COUNSEL

The Columns

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Let's talk about inflation. I weigh 150 pounds. Well, it depends on the scale. My mental scale says it's 150 pounds exempting Magnums and Wicked Weed Pernicious. Let me explain. Magnums are chocolate covered ice cream bars and Pernicious is the greatest beer produced today. Give the Magnums a try and you can thank me later.

In reality, my weight is 160 pounds, and I don't get to deduct the weight caused by my intake of ice cream and beer. If this sounds familiar it should. The September consumer price index (CPI) showed inflation spiking 5.3% over the last year. The Fed advises us not to worry because the real number is only 4% once you *back out* food and energy. You know, the things we use every day to conduct our lives. The Federal Reserve reiterates this inflation is transitory and prices will drop again. I'm not so sure. My $60 gas fill up last weekend didn't feel very transitory.

A large inflation component is the cost of housing. If you've bought or sold a home this year, you know housing inflation is rampant, but the CPI understates this. The Wall Street Journal showed that apartment rents increased 10% year over year, but the CPI showed only a 3% rise. Who's right? Given what I've seen, I'll side with the WSJ on this one. By the way, the Journal's number was based on an analysis of 13 million apartment units.

In spite of the real-world inflation, the Fed is still not raising rates. I just refinanced at 2.125%, and never thought I'd see that. In the wake of the CPI data, Ten-year US Treasury yields actually dropped to 1.25%. My issue with ultra-low rates is that they skew the flow of money.

Investors are sometimes more willing to speculate. Just check out GameStop and its current PE of 290. The number of stocks that are trading for more than 10 times annual revenue is at a level not seen since the 2000 tech bubble.(*MarketWatch*) This doesn't mean the market has a reckoning on the way, but it may mean that the growth portion of the market is overpriced. My outlook is not negative, but we may be due for a small selloff.

The good news is that any potential selloff may be a launch pad for a strong finish for 2021. The market was up 20% year to date on August 31st. What happens now? The Standard and Poor's data shows that we've seen this 7 times before and the market finished the year with a gain in 6 out of 7. The average gain through year end was 3.3%. If that sounds low, note that it includes the one negative finish: 1987.

I was around for that one and the market completed a 25% loss for the period. If you back that one out, the average gain jumps to 8%. One thing many forget about 1987 was that while the selloff was horrible: the market dropped 22% in one day. However, the market bottomed for good on Friday, December 4, 1987, and started a bull run that notched a 59% gain.

It took Saddam Hussein's tanks rolling into Kuwait in August 1990 to end that run. Back in 2021, the economic data is still solid, and we feel that could be the case for the next year. With that positive backdrop, we feel the downside could be limited, so our view is to buy any selloffs to lay a foundation for 2022.

18 months later and Covid is still making European travel difficult. But what if I told you that you could experience "Europe" without leaving the state of Texas? Let's call it the redneck European tour. As a North Carolina native, I can use the term redneck since I actually am one. The tour will take in all the hotspots including Paris, Moscow, Berlin, Vienna, London, and Dublin. Your drive time is 17 hours and 1041 miles long. Yes, everyone of those cities is in Texas. Happy travels, like the Magnum bars, you can thank me later. 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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