CAPITAL INVESTMENT COUNSEL

The Columns

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I think the market has a discipline problem. When I was a kid, I liked to misbehave. It's part of being young. When my mother caught me, she would give me "that look" and say I'm counting to three and suggest that you stop what you're doing before I reach three. Thinking back, I don't think she ever reached three when she was dealing with me. Her record spoke for itself, I did not want any part of what happened after 3. My sister was different story, but that's a story for another time.

The Federal Reserve and Jerome Powell talk a lot about inflation. Powell uses words like temporary and transitory but the prices we're paying for goods and services don't feel transitory. My favorite cold brew coffee (Slingshot, thanks for asking) just went from $8.99 to $11.99. I'll save you the trouble of getting out your calculator, that's a 33% increase. The Fed says they'll raise rates when the time is appropriate but when exactly is that? The market doesn't believe Powell and the Fed will ever "count to three" to channel my mother's disciplinary style. The market thinks rates are staying lower for longer. In late November, Gold zoomed to a five-month high, and crude oil is up 70% this year. In response, the Fed has kept rates near zero.

Without the threat of discipline in the form of higher rates, the market figures it can get away with a lot. That lack of discipline has helped fuel a boom in speculative stocks. It's one thing for Microsoft to trade at 36 times earnings and 12 times sales. That's feels expensive but their growth has been amazing. Let's compare that with Snowflake. It's trading at 79 times sales, but it has no PE. There's no E to compare as Snowflake hasn't made any money. It feels a bit frothy.

The economy is booming. Employment is heading higher, people are traveling and spending again. It's great to see, so what's the Fed waiting for? The consumer price index came out last Thursday with the highest reading since 1990. Interest rates dropped in response. 1990 was a long time ago. Mariah Carey and Bon Jovi were in the Billboard top ten, and the UNLV beat Duke in the NCAA finals. Yes, Coach K was in charge back then and it was every bit as fun to watch Duke lose. In 2021, I enjoy having a smaller mortgage payment thanks to lower rates but don't care so much for a money market that pays near zero on my cash. The price of everything else seems to have gone up.

I don't think this story has a bad ending, but we may see a shift in which stocks plays the hero. It feels like some of the winners of the 2021 market have a foundation built on low rates. There seems to be some similarity between the movement in high priced tech stocks and interest rates. Rates climbed strongly from November 2020 through May 2021. Delta Covid took a bite out of economic growth, and the slowdown drove rates lower.

For the last 6 months, low rates have been giving a helping hand to tech valuations and here we are. So, what happens as Delta continues to fade and the world gets back to normal? Things are getting better quickly. On Tuesday, retail sales rebounded to the highest level since Delta started. As rates tick higher, is Rivian still worth $140 billion after selling only 156 trucks? It should be fun to watch.

I love fall. I love the low slanting light, and the crisp mornings. I also love that when the market has had a strong year like 2021, history has been kind in the past. The S&P had a solid double-digit gain coming into November. That's happened 8 times. In all 8 times, it's finished the year positive for November and December with an average gain of 6%. Kudos to Ryan Detrick at LPL for the stat. If you're feeling negative, it may be too early to put on that bear costume yet. Happy Thanksgiving everyone, 2021 has been a wild ride but I'm thankful for how much better it's been than 2020. Just think how much further along we'll be this time next year. 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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Capital Investment Counsel, Inc. 100 E. Six Forks Road, Ste. 200; Raleigh, North Carolina 27609

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