Marketline April 2022

Stocks:

Last month, despite positive market returns, we wrote: "While many pundits are claiming that the economy is strong and can withstand higher rates, we see matters differently. The economy may in fact be strong, but trends in some indicators are pointing down. Even if we are able to make it past a Fed error and escape a recession, it is likely that the peak in earnings is either upon us, or nearing. The double threats of higher rates and diminishing earnings growth can be difficult to surmount."

In April, earnings reports from some bellwether stocks were not as strong as expected. Amazon reported a loss; other companies' forecasts left much to be desired. Inflation did not abate; and the Fed became more hawkish. Consequently, the downtrend in place until March's slight rebound continued with a vengeance. The damage was particularly onerous in speculative stocks and the tech sector. Stocks like Rivian, the electric truck maker, with no earnings and scant revenue, experienced true bear markets in a matter of days. The S&P was down 8.8%, the Dow fell almost 5%, and the Nasdaq plummeted 13.3%. Overseas things were not much better, with Canada's market down about 5%, Mexico sinking 9%. Only Europe closed about flat. We come into this fracas with above average cash positions, generally, having chosen to sell down several expensive stocks over the last four months. As mentioned in previous letters, some accounts will be rebalanced toward bonds, but much of the cash is likely to go towards new stocks as opportunities arise in a correction.

We've been asked how long the decline will last. We don't know. Much depends on what the Fed does and how the economy adjusts. The latest GDP report was negative, indicating the economy contracted in the first quarter. Excuses were given for why the number was an anomaly, the bond market did not react and the Fed reiterated full steam ahead. Then there is the war between Russia and Ukraine. With the West arming Ukraine endlessly, the conflict will be prolonged, perpetuating this source of uncertainty for investors and humanity as well. We have spent some time considering what could go right from here. Other than a resolution to the war, here are a few things:

1. Inflation abates.
2. More people decide to rejoin the labor force, easing employment shortages.
3. China decides to soften its 'zero covid' policies.
4. The shift from spending on things to spending on services eases supply chain issues.

While we're not holding our collective breath on any of these, each of them does sport a probability greater than zero.

Bonds:

Yields took another significant leap upwards last month, causing more losses in bond values. The long Treasury rose to 3% - which is exactly where it traded on April 30, 2019, three years ago. Short term interest rates rose as well: the one year note closed at 2%. The yield curve is no longer inverted, but it is flat as Texas from five years out.

Rumors are that the Fed plans a 50 basis point hike in early May, which amounts to 0.5%. The expectation is that hikes will continue at nearly every meeting this year. Eventually this will start showing up in yields on money market funds, but we're not waiting around for that to happen. We've started investing some accounts' large cash balances in short term Treasury bills. At least there we can obtain 0.3% to 0.5%, better than the 0.0% that money market funds pay now. If you're drawing money out monthly, we're less likely to do this, but take heart, it should not be too long before cash balances start to pay more than zero. On the flip side of this, mortgage rates are also rising. We hear that 5% for a thirty year fixed loan is standard, and rates are likely to rise much higher than that soon. While home prices are not reacting to this lack of affordability yet, sales are slowing.

In other bond news, municipals are offering 4% tax free in longer maturities now. Just last December it was difficult to find 2.5%. The swift rise to 4% highlights the suddenness of this move in rates. For new bond investors, this leap is a blessing, but for existing portfolios, those bonds are worth less now. Cash flow, though, remains the same.

*Marketline Monthly is produced by **Cascade Investment Advisors, Inc**. We specialize in value investing for individuals. We apply our approach across markets, looking for low-priced securities that offer above-average potential. We use imagination and hard work to bring performance and personal service to our clients. Phone 503.703.3622 (Michelle); our website is www.cascadeinvestors.com. A full list of securities we invest in is available on request; mention of specific securities is not investment advice; such investments may or may not be profitable. Index returns quoted are price only.*