

Marketline November 2023

Stocks:

Last month concluded a two-month decline in stocks that quit almost on the dot at the beginning of November. Not only did it quit, but November gave us one of the most robust periods on record for stocks, with the Dow and the S&P up almost 9% each, and the NASDAQ adding almost 11%. Many entire years have seen worse returns on stocks than this one month, so to rack this up in a single 30-day period is unusual. It is worth mentioning at this late date in the year that the index returns have been substantially influenced by technology stocks. Since the beginning of the year, the seven largest tech stocks are up 71% - an eye-watering number - while the other 493 companies in the S&P are up 6%. Small-cap stocks in particular have seen their worst performance relative to their larger peers since 1998, which was quite a crummy year.

Our primary international trading partners - Mexico and Canada - fared about as well as the US. Generally but not always, when the US performs well, that benefits our neighbors. Mexico in particular is seeing keen interest on the part of companies that want to "near-shore" production, away from Asia to a geography that's easier to access. Europe was not as fortunate as North America last month, with stocks rising barely 2%. European countries are slipping into recession, as high energy prices play havoc with manufacturing and consumer sentiment. In Germany, the cost of electricity is roughly four times what we pay in the States. Industry bears the brunt of this expense because subsidies help alleviate the costs for households. However, evidence shows that industries are closing plants and shifting production to other countries to reduce costs. Longer term, that threatens Germany's illustrious economy which has heretofore been the largest in Europe.

Like October's downward action, the explanation for November's upward market action lies in one of the primary drivers of stock valuation: interest rates. As we will note below, rates fell fairly dramatically during the month. This volatility is unusual, but it's a hallmark of our economy for the time being as the Fed grapples with how to address inflation. Despite November's surge, we were able to find a couple of new names to augment our buy list - Diageo and ePlus. Diageo sells spirits including Johnnie Walker, Guinness, and Bailey's. ePlus is a technology consultant helping medium and large businesses administer and upgrade all manner of technology. As always, we'll gradually make purchases of these names where appropriate.

Bonds:

As fast as rates rose in October, they sank in November. The long bond yield dropped from 5.09% to 4.49%. The all-important ten year ended at 4.32%, down from 4.93%. This will prompt a decline in mortgage rates eventually. There wasn't much action in the short end - and there won't be until the Fed decreases rates. Sector news has changed again. The big rally in November took most bonds up in value, but municipals really skyrocketed, having their best month since 1986. Lucky for us, a few stragglers - Pearland, TX and Bromley, CO - hung close enough to our 5% bogey that we were able to make a few purchases before turning elsewhere.

Good quality corporate bonds are still worth a close look. Triple-B bonds remain in the 6% camp. I haven't confessed my wild bond theory to many of you yet, but I'm ready to publicize it here: I think in years to come investment-grade corporate bonds will not experience the dramatic spread-widening that we have seen in past recessionary economic cycles. What does this mean?

1. Spreads are the difference in yield between any bond and its similar-maturity Treasury. So we measure a ten-year corporate against a ten-year Treasury.
2. Spreads widen when everyone is scared of a recession or credit crunch. Then, investors want to own government debt, not Starbucks' debt, when things get tough.
3. Why won't we see widening? Corporations have generally been better behaved than our own government, which continues to accrue deficits. So we're saying that investors may come to view Starbucks' debt more favorably in a downturn than in the past.

Time will tell if we are right, but in the meantime, we see plenty of value in company debt these days.

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