Marketline May 2024

Stocks:

May provided almost enough positive return in stocks to make up for April's decline, but results were uneven. The Dow – that stodgy index that somehow continues to be relevant despite its relative paucity of technology stocks (only six out of the thirty components) – was up about 2%; the more tech-saturated S&P rose 4.8%; and the NASDAQ increased almost 7%. You probably don't need me to tell you this array of numbers means technology drove returns this month, nearly all on the heels of good results from Nvidia, the king of AI chips. Overseas, returns were more modest, as we'd expect. When risk appetites are high and tech performs well, overseas markets tend to be left behind. The Canadian market rose about 2.6%, and European stocks were up 1.6%; remember that translating those returns back into the strong US dollar gives the numbers a haircut. In Mexico, returns fell 2.8% as investors worried about the now-settled election which is not necessarily promising for business or democracy there.

Quarterly earnings reporting season is largely behind us and overall results were a bit of "hit and miss", but interest rates remain a definitive drag. We think that's why investors banked on the "tried and true" tech sector in an uncertain spring season – it's easier to own what has worked in the past. We've generally chosen to go in the opposite direction by trimming tech holdings, giving up a small slice of performance in return for controlling risk.

Out in the broader economy, government expenditures for infrastructure, and subsidies for manufacturing and purchases of climate-friendly items have done a yeoman's job of helping us avoid a recession. But the consumer is sputtering a bit after a strong performance over the last several years: credit card debt is rising and the savings rate is falling. Industrial production has been uneven as well. The labor market – which everyone likes to cite as indicative of economic health – is a notable laggard, showing distress only after a recession has begun. We're not seeing enough signals to call a recession yet, but a slowdown is afoot. If this manifests in earnings reports, we might have an opportunity to finally expand our buy list with a few undervalued stocks, but so far, not much luck on that score.

Bonds:

Interest rates meandered down across the board last month, a bit of a miracle since both Jamie Dimon (CEO of JP Morgan) and Neel Kashkari (from the Fed) actually made mention of a possible rate *hike* from the Fed, rather than rate cuts. I thought I was the only one considering that possibility, but apparently not. In any case, the long bond ended at 4.65%, down from 4.78%; the ten-year – important for mortgage rates – dropped to 4.5%. When we view the last six months' worth of these market letters we've written, the bond market has been trendless: a little up in yield here, a little down in yield there. Only better inflation numbers can break this stagnant pattern.

In the trenches, where we spend a part of every day, we continue to see value in corporate bonds – an opinion that virtually none of our peers shares – and we are wary of municipals. In the corporate segment, our fondness is simply a matter of practicality: no, they're not cheap - in fact, they are expensive - but the nominal yields are between 5% and 6%. That level is a far sight better than the 3% we were seeing a few years ago. Five percent or more can make a material difference to client cash flows.

On the municipal side, I'm wary because I expected the recent proliferation of infrastructure projects to provoke a lot of bond issuance, which raises supply. And that's exactly what's happening. We are awash in new municipal debt. That's pushing yields up and prices down. At some point, higher yields will become "worth it" but we're not there yet.

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