

Stocks

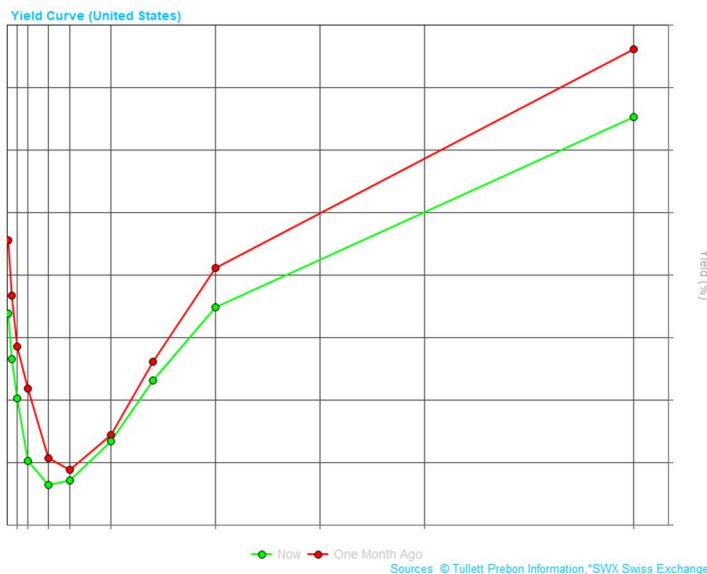
I'm starting to sound like a broken record – sorry! But once again, stocks put in a strong showing. This time, the tech-heavy Nasdaq set the pace, rising 5.6%, while the S&P – with a considerable dollop of tech stocks itself – was up 3.5%. The Dow was the wallflower, posting “only” 1.9% - a price increase that would be considered terrific if it weren't for its more illustrious peers. Overseas, results spanned a similar range, with Canadian stocks up 5.1%, Mexico's Bolsa rising a very strong 7.2%, and the FTSE index of large European stocks lagging at 1.8%.

Last month, we wrote: “Stocks' progress has been met with concern, doubt, skepticism, and mistrust”. It's worth considering: what is the opposite of concern, doubt, skepticism, and mistrust? The answer is complacency - or its sidekick, enthusiasm. Either will do for our purposes today, which is to remind investors that as soon as we begin to believe that stocks will go up forever, or that we should “get in” before the run is over, the market will teach us a lesson – and not a pleasant one – by sinking. While we're not market timers, we've seen over and over that an “everyone in the pool” attitude is a setup for a temporary decline.

How do we know everyone's in the pool? Usually, strange things start happening: the stocks of financially precarious companies rise a lot; everything else rises a lot; people borrow money to buy stocks or options; no one is recommending selling anything; good news is good for stocks and bad news is good for stocks; risk in other markets becomes mispriced. Today, we have a few of these pillars in place, but not all of them. As warning signs proliferate, we will be considering how to deploy cash into price corrections.

Bonds:

The Fed finally cut rates, one step toward aligning short-term interest costs with the market. More cuts are expected. If those materialize, great – but things could turn dicey if the Fed stands pat next time. As an aside, the Fed's exhortations about being data-driven are not particularly impressive. Rates on short bills remain below the fed funds rate.



This chart shows where rates are along the curve. Does this look normal to you? It's not. That hook on the left side is not normal; that is where the Fed is calling the shots. The rest of the curve is determined by market forces. Do we really need data other than the market, which has been saying for many moons now that the Fed is keeping rates too high?

In other news, Microsoft has come to market with bonds lately, and the interest rates they are paying are less than what the US Treasury is paying. Ok, this is not the first time I've seen a corporate bond yield less than the Bonds of the Land, but the occurrence is rare. It buttresses our belief – which we have described here and elsewhere – that certain corporate bonds may become more desirable than our government debt – on a

permanent basis. Microsoft runs a tight ship: it doesn't spend endlessly, it doesn't issue bonds nearly every day of the week, it doesn't shut down because its executives fight with each other. Why shouldn't it be rewarded with low interest costs? While we're not buying MSFT's bonds, we do buy many other corporate issues that are also benefiting from their companies' relatively good behavior.

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