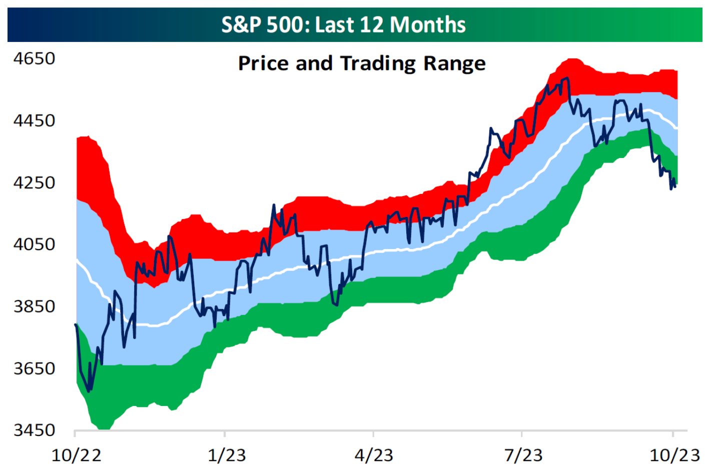
Capital Ideas

October 9, 2023

Capital Ideas Advisors
12720 Hillcrest Rd., Suite 910
Dallas, TX 75230

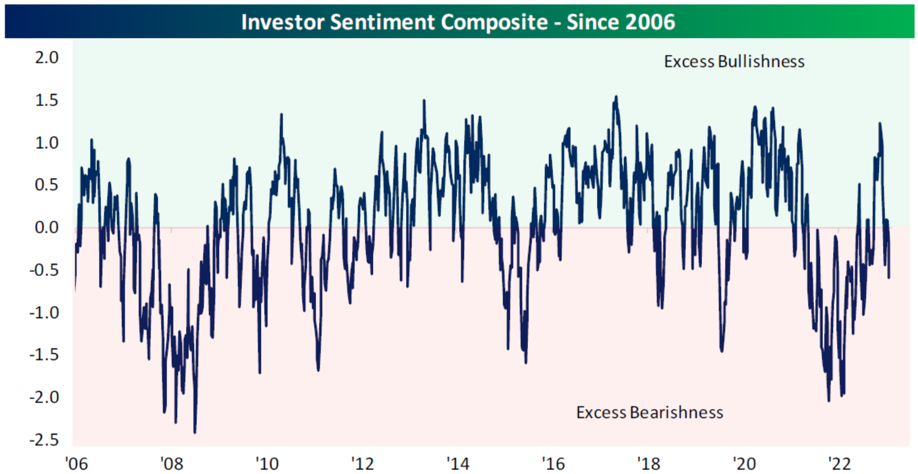
Dear Reader,



Source: Bespoke Investment Group

Long time readers of our monthly missive know that we always try to balance stock market technical conditions with fundamental factors when we are evaluating current and perceived future investment decisions. Currently the equity market is more oversold than it was on the bottom it made in October of 2022. And while stocks decline bond prices are falling precipitously as interest rates spiral higher in a global bond market selloff. Investors are selling and fleeing for the perceived safety of money market instruments. During this turmoil we are reminding ourselves of what Warren Buffet said, "be greedy when others are scared." In our opinion these near panic conditions are the prelude to that time when we should be greedy. And while September may be the "cruelest month" for stocks, October is known as the "bear killer," the month when stocks usually bottom. But before we can begin committing some of your cash reserves to new investments we want to review the underlying causes of the current market turmoil and assure ourselves they are about to be ameliorated.

The most obvious factor influencing the markets is interest rates. Reviewing recent levels of the 10-year US Treasury note we note that each time its rate rose above 4%, in September 2022, February 2023, and July 2023, stock prices soon tumbled. The current stock swoon which began in July of this year has extended into October as the 10-year rate continues to increase. This is the fault of the FED, but we believe the financial medias current fixation on FOMC meetings and Chairman Powell's pronouncements is misdirected. While such observations make timely news fodder, in our opinion the real culprit behind todays rising rates is central bank quantitative tightening (QT). While central banks around the world are all simultaneously selling bonds our own Federal Reserve is also selling. To reduce its balance sheet the Fed is selling long term debt while domestic banks and foreign buyers, particularly China, have drastically reduced their buying. We believe this



** Average of z-scores of AAII and Investors Intelligence bull-bear spreads and NAAIM Exposure Index.*

Source: Bespoke Investment Group

is the real unrelenting pressure on interest rates. In our opinion it is also the most crucial factor which will hold rates "higher for longer." As you know higher interest rates normally translate into lower stock prices through the mechanism of price/earnings ratio compression. As long as the Fed engages in QT and rates remain at current levels, or higher, p/e's will remain compressed. As we have pointed out many times, without the aid of expanding p/e's stock prices will only rise at a rate directly proportional to earnings growth rates. And earnings growth is difficult in a slowing economy with inflation pushing up the cost of both labor and materials.

While the economic factors of inflation and interest rates dominate market fundamentals the technical factors are important for our decision process. Currently the most important technical factors are investor sentiment and relative market pricing. In the first paragraph we briefly mentioned the elevated level of investor fear. Exacerbating this fear are various headlines concerning the recently postponed government shutdown, the situation at the Southern border, lower savings rates, and higher mortgage rates. The anxiety they create escalates uncertainty and markets can discount anything but uncertainty. The current excessive uncertainty produced excessive selling which created the oversold condition the market is in today. Experience has taught us that oversold markets can become more oversold. Therefore we are waiting for the point of maximum fear to exercise our greed. Certain technical indicators such as the trading range chart in this letter, expanding new lows in price or the relative level and velocity of change in the VIX aid us with this determination. We hope to be able to identify that point in market prices when fear is the greatest. Once we are confident in that judgement we plan to commit significant portions of your cash reserves back into securities suitable for your account. In the meantime we plan to leave excess cash in the higher yielding money market fund you are currently invested into.

As always, we thank you for your patronage and encourage you to call us with any questions or concerns.

Sincerely,

CJ Brott

Karen Burns

Andrew Kerai