Capital Ideas

December 8, 2023

Capital Ideas Advisors
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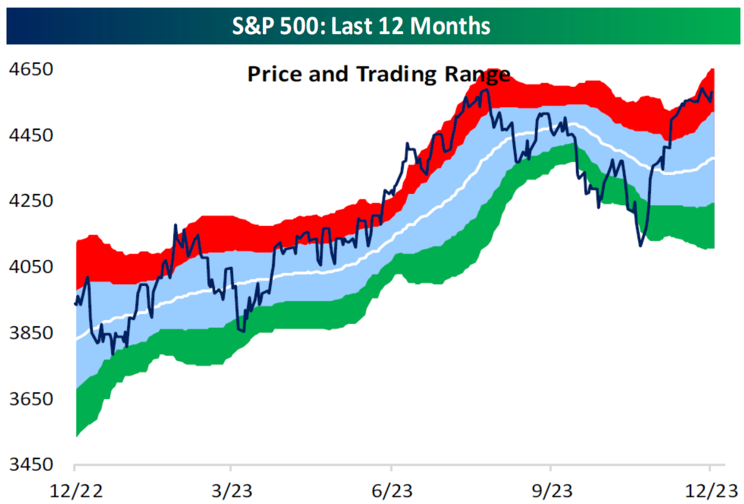
Dear Reader,



Source: Bespoke Investment Group

This year's economy and stock market have much in common with the story of Goldilocks and The Three Bears. Just as some porridge was too hot, too cold, or just right, we can say the same about interest rates, inflation, and stock prices. Early in the year inflation was too hot and investors feared the Fed's attempts to cool it would push the ten-year Treasury interest rate above 6%. In the Spring rates did heat up and the ten-year rate briefly exceeded 5%. Subsequently the stock market cooled off and declined sharply recovering in the late Fall. Throughout the spring and summer investors remained depressed as popular financial news anchors and their guests expounded on the possibility of inflation reaching levels not seen since the 1970's. The pundits were wrong. Currently the core PCE level is no longer too hot with a reading of 2.3%, close to the Fed target of 2%. With inflation cooling ten-year rates are currently below 4.2% and expectations are for the Fed to continue lowering the heat on rates several times next year. By themselves sharply lower rates of interest and inflation would cause the casual observer to conclude the economy is exceedingly weak and on the verge of recession. However, in the third quarter the United States reported GDP growth above 5%, and globally PMI (purchasing managers indices) as reported are quite strong. The current outlook for robust growth in a disinflationary economic environment which is not too hot or cold is known as a "Goldilocks Scenario." It has always been extremely positive for stocks. Besides a favorable and improving economic environment, and unnoticed during the six-month sideways market, technical conditions have been improving.

The most convincing indicator of future improvement in stock prices is the

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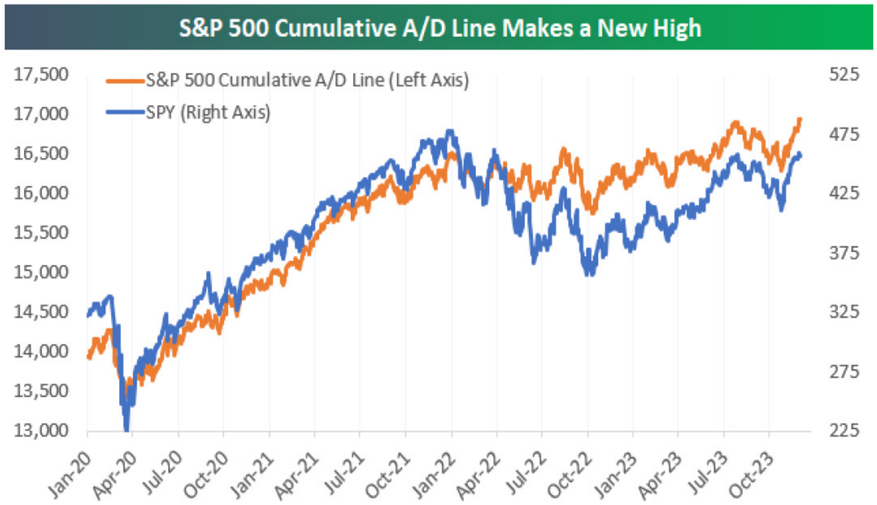
cumulative advance/decline ratio. As illustrated in the accompanying chart while stock prices have gone sideways throughout the year the A/D ratio has been improving the entire time and has now broken out to new highs. In our opinion this breakout is an extremely bullish development. Almost without exception new highs in this indicator have preceded new highs in market prices.



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As long-time readers of this missive know we value agreement between economic and technical market conditions. Agreement of these two areas tends to generate the most reliable investment signals. Our experience in investment markets has taught us the market tends to anticipate future economic conditions and moves well before any improvement in the economy is obvious. Normally a stronger economy generates improving financial performance by smaller companies and eventually their stocks. Signals are indicating that next year's economy will be good. The markets A/D line is signaling that anticipation as the stock market broadens out with participation by an expanding list of companies.

Until recently market advances have been dependent on performance by the seven largest company stocks. Smaller stocks failed to participate or declined. With the current improving conditions we are seeing opportunities for investment in a broader universe of stocks and ETFs suitable for new investment. As these opportunities come into view, we intend to continue investing your cash and cash equivalents in them. As always thank you for the opportunity to aassist you with your investment needs. Please always contact us directly with any of your questions or concerns.

Sincerely,

CJ Brott

Karen Burns

Andrew Kerai