

FOCUS NEWSLETTER

A TIMELY UPDATE ON THE ECONOMY, FINANCIAL MARKETS AND INVESTMENT OPPORTUNITIES

APRIL 2024

Still A Healthy Economy

The economy continues to show strength.

Fourth quarter GDP was revised up to 3.4%. The revision reflected increases in consumer and business spending.

At their March FOMC meeting, the Federal Reserve's (The Fed) committee also painted a promising 2024 by revising GDP growth predictions upwards and reducing unemployment expectations for the year.

The consumer price index (CPI) increased 3.5% in March. It was higher than expected, and higher than the previous month. The cost of services – rent, car insurance and transportation – continued to rise.

We've noted before bringing inflation further down to The Fed's 2% benchmark will get harder. The Fed remains focused on service inflation, which may fall when personal consumption loses steam. Consumer savings has been dwindling and credit card balances are rising at higher rates. Meanwhile, overall inflation should remain elevated this spring due to rising energy prices.

Still "Higher For Longer"

We noted at the end of 2023 Fed rate cuts were on the horizon. However, we didn't think they would occur in the first half of the year. We also were skeptical of the euphoria in the media that the cuts for the year could total as high as 1%-2%.

Market-based odds for a March cut were at about 65% at the end of January. The odds for a June cut were roughly 20% due to recent strong employment data and stubbornly high inflation.

Our headline remains "Higher For Longer" with regards to overall inflation and interest rates.

The economy can perform reasonably well in an environment when the 10-year Treasury is in its current range of 3-6%.

KEY DATES

- 4.5 Unemployment Report
- 4.0 March CPI
- 4.25 GDP 1Q Advance Estimate
- 5.1 FOMC Press Conference
- 5.3 Unemployment Report
- 5.15 April CPI
- 5.27 Memorial Day
Stock Market Closed
- 5.30 GDP 1Q Second Estimate
- 6.7 Unemployment Report
- 6.12 May CPI
- 6.12 FOMC Press Conference
- 6.19 Juneteenth National
Independence Day
Stock Market Closed
- 6.27 GDP 1Q Third Estimate



It's still well below the average of the last 60-plus years.

The lesson is that the market is not particularly good at predicting Fed moves until just days prior to meetings. It is hard to imagine the Fed is in a rush to cut rates with strong employment trends, inflation roughly 75% above the 2% target, and decent reported economic growth.

Result: The Fed might cut rates closer to .50% during the second half of this year, leaving bond yields near their current range. Timing for this cycle's first rate cut is tricky as The Fed does not tend to change rates right before a Presidential election.

A New Era of Productivity

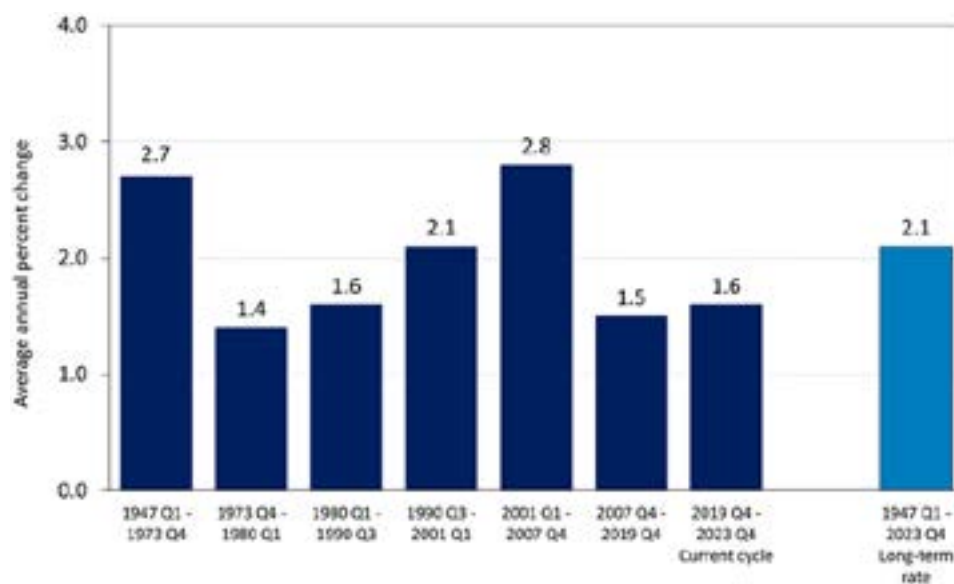
Most economists predicted modest growth or contraction in 2023 due to high inflation and the prior rapid increase in interest rates.

But that wasn't the case.

There were several factors that led to a stronger economy: the employment picture was strong, wages grew, and consumers spent at relatively high rates.

Of particular note is productivity improved meaningfully. Workers and companies were more efficient in 2023 than during the pandemic. Generating more output per hour, productivity rose 3.2% in the fourth quarter. The growth was well above the post financial crisis trend level of 1.5% and even better than the long-term post WW2 average of 2.1%.

Productivity change in the nonfarm business sector, 1947 Q1-2023 Q4



SOURCE: U.S. Bureau of Labor Statistics

LAST UPDATED: 03/07/2024

As productivity rebounds from Covid levels, the economy can expand absent of inflation. With increasing productivity companies can make the same or larger profits without raising their prices.

This trend should continue. Increased usage of technologies streamlining work leads to more productive hours worked. Artificial intelligence has the promise to further boost productivity.

Investing In An Election Year

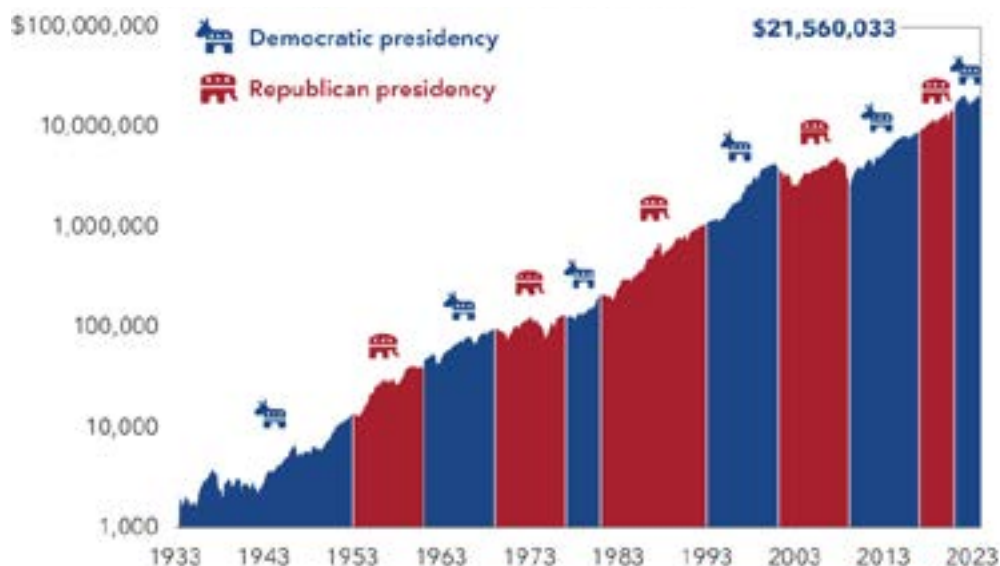
Election years can make investors nervous. Rightfully so as Presidential campaigns (and the media) can amplify what's wrong with our country and economy.

A common mistake investors often make during election years is timing the market. An analysis conducted by The Capital Group shows investors since 1992 tended to move more money into conservative cash and/or money market funds leading up to elections.

The study calculated portfolio returns after the last 23 election cycles assuming a four-year holding pattern. Investors who were fully invested in equities or made monthly contributions to equities (versus staying in cash) had higher average portfolio balances over the full period nearly 75% of the time.

The party that wins generally doesn't dictate long-term investor returns. Since FDR held office, we've had 7 Democrat Presidents and 7 Republicans. Throughout this period the market has experienced double digit returns regardless of Party affiliation.

Growth of a hypothetical \$1,000 investment in S&P 500 Index



SOURCES: Capital Group, Morningstar, Standard & Poor's. As of 31 December, 2023. Dates of party control are based on inauguration dates. Values are based on total returns in USD. Shown on a logarithmic scale. Past results are not predictive of results in future periods.

Bottomline: Stick to long-term investing principles even during volatile market election years.

Looking Ahead

Many predicted that 2024 would be volatile. The first quarter had some wild swings. Wars in the Middle East and Ukraine, a ramped up Presidential election, artificial intelligence (AI) hype and Wall Street bets on rate cuts are causing an emotional roller coaster.

Emotions can be an investor's worst enemy.

In this environment investors should be wary of certain cycles that may be nearing inflection points and stick to sound investment principles. Over the long-term, returns are driven by sound fundamentals and not the latest clamor.

Broader Market Value – History suggests we are near the end of a mega/large cap cycle that has outperformed small caps by approximately 80% annualized over the last 10 years. Valuations of the top 10 stocks that make up approximately one-third of the S&P 500 market cap trade around 25-30 times earnings. There's more value in mid/small caps than expensive, shiny large caps.

Dividend-Payers On Sale – Valuations for high dividend paying stocks are approximately 15% below the market average since 1980. Dividends generate income, and when reinvested, can double/triple an investment through long-term compounding. Approximately 60% of our current holdings pay dividends.

Financially Strong, Innovative Leaders – Leaders in growing, profitable niche industries are attractive. We are investing in those that generate excess cash and use it to reward shareholders and reinvest in future growth.

Many of our holdings can benefit greatly from artificial intelligence (AI). For example:

Technology: Chip manufacturers are grossly overpriced. Instead, we own two significant leaders with great value in the tech space. InterDigital owns a high proportion of patents in 5G and 6G technology that are used to

transfer big data generated by AI. Qualcomm is inventing, developing, and commercializing power-efficient on-device AI, edge cloud AI, and 5G.

Healthcare: Pharma companies like Bristol Myers Squibb and Exelixis are exploring ways to use AI to scan hundreds of thousands of molecules and chemical compounds to find solutions quicker. This has the promise to save costs, get treatments to the market sooner and grow revenue.

Media: AI can benefit our local media companies such as Nextstar and Gray Television. By processing huge amounts of data, they can provide advertisers higher quality data on their target audiences. This provides Nexstar and Gray with more opportunities to sell more inventory at premium prices.

Check It Out

We refreshed our website last month.

The new site was designed to better explain our investment philosophy and approach, i.e., how CMC invests in highly selective companies possessing superior cash flow and sustainable growth potential.

Many have heard us call them CASH COWS. The screen shot here describes how they have a greater potential to mitigate downside risk and generate larger long-term returns.

Our strategies/model portfolios also are on the site. Visitors can easily view the objectives, key characteristics and performance of each model.

[Click here to check it out.](#)





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About: The Capital Management Corporation

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CMC is 100% employee owned and operated. We are one team, the same team; we are a family. This shared knowledge fosters camaraderie, communication and collaboration. We have a shared vision and passion for excellence. There is ownership over decisions, results and performance.

Together, we serve as our clients' fiduciary. We focus on growing wealth, preserving capital and generating rising, recurring streams of cash income. We greatly appreciate your confidence in our team, services and results.

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