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VICTORIA Capital Management, Inc.

Market Musings

A newsletter brought to you by Victoria Capital Management, Inc.

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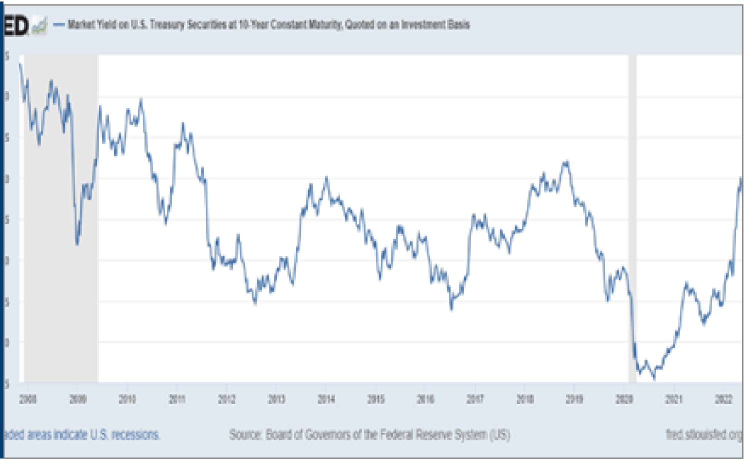
The chart shows the yields on 10-Year Treasuries starting from 2007 just prior to the recession of 2008-2009 and finishing to the end of October this year. The yield has declined over the past 15 years and only recently has started climbing to more normal levels.



aded areas indicate U.S. recessions.

Source: Board of Governors of the Federal Reserve System (US)

A Return to Normalcy

Earlier this year we compared the 2020-2022 pandemic and subsequent meltdown of the stock market to feasting –read overindulging—on Thanksgiving Day and recovering from the resulting gastrointestinal pain afterwards. The $7 trillion infusion to bail out the economy changed the behavior of consumers and investors leading to enormous speculation in both stocks and real estate. This speculation contributed to the inflationary surge in 2022 and the Federal Reserve's response to that surge with a policy of driving interest rates higher by increasing the fed funds rate (the rate that banks lend to each other) rapidly. The impact of that rise, as far as consumers were concerned, was the surge in mortgage rates from 3% or lower in 2021 to over 7% recently. Most home buyers have a maximum monthly payment in mind for a home purchase so the rise in mortgage rates squeezed them out of the market. Housing prices have already turned down and are likely to continue to fall until some sort of equilibrium is reached. Historians will look back over the period 2009-2021 as a time when borrowers experienced a "golden age" of record low interest rates. If inflation remains a threat, monetary policy will normalize interest rates at current or higher levels for the foreseeable future. Forecasts of another 75-basis point increase in the fed funds rate this week and then another 50-basis point increase in December will push interest rates higher and bond prices lower. Yet these policies are only bringing interest rates back to levels that prevailed in the previous decades before 2009. The fall in the stock market has taken the market P/E ratio back into an area that would be considered normal given the history of the modern stock market. Oil prices that surged above $125 this Spring have fallen back into the mid-80s, closer to what we consider to be a normal range for this critical commodity. Natural gas prices also have fallen back from recent highs as supplies have increased rapidly. We are headed into Turkey Day again so a replay of the past "economic" thanksgiving should stay where it belongs—in the past.

***"The only thing you can be sure of is that there are times where large numbers of stocks are priced too high and other times when they're priced too low."* -Benjamin Graham**

Market Commentary

After a rough year so far, equity markets rebounded strongly last month with the DJIA posting the best October since 1976! Shrugging off disappointing "Big Tech" earnings and still-elevated inflation, the S&P 500 had its best month since July, with a total return of 8%. Outside of the tech titans, earnings figures have been encouraging and smaller companies have been riding the positive sentiment to double-digit gains. The S&P MidCap 400 and S&P SmallCap 600 were up 11% and 12%, respectively. Foreign equities also finished out the month in the green while emerging market stocks finished down—despite very strong returns in Brazil and Chile. Bonds declined across the board with long-term issues suffering the most while the dollar took a breather from its ascent so far this year. Many market observers believe such a turnaround is indicative of a new bull market even though there remains the ongoing uncertainty of interest rate hikes and the continuing war in Ukraine.

Data from Birinyi Associates indicates that U.S. companies have announced stock buybacks totaling $1 trillion so far in 2022, up 8% from a year ago and on course for an annual record high, according to Bloomberg.

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