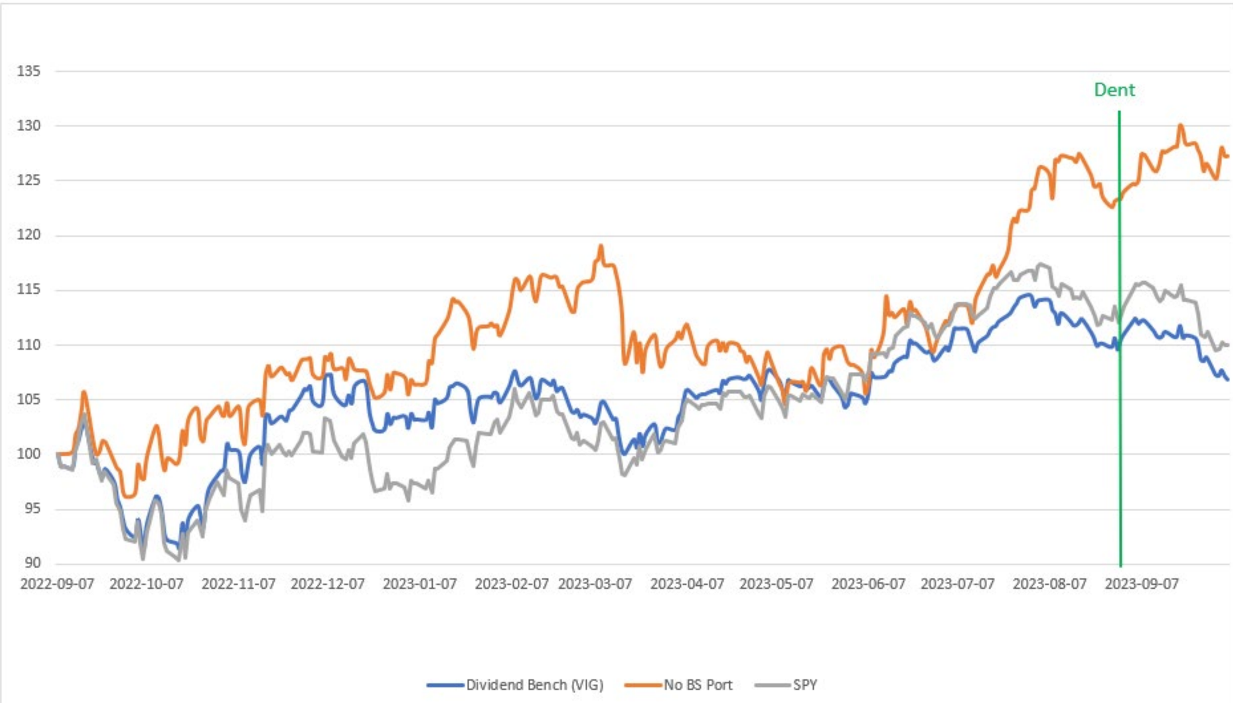
October 9, 2023

The NO BS Growth and Income Portfolio

By John Del Vecchio

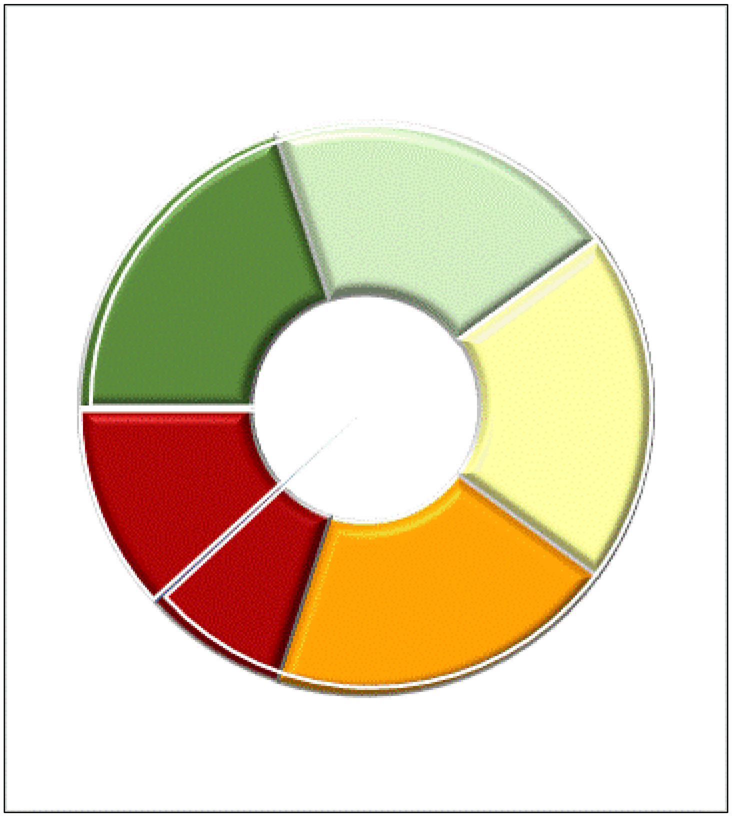


New trades this week: None.

Current Portfolio, October 9, 2023

Ticker	Name	Return	Days Held	Sector
ABM	ABM Industries, Inc.	5.65%	25	Business Services
AVT	Avnet, Inc.	0.35%	25	Technology
CGEAF	Cogeco Communications, Inc.	-11.34%	53	Telecommunications
ETD	Ethan Allen Interiors, Inc.	28.52%	399	Consumer Cyclicals
HVT	Haverty Furniture Cos., Inc.	6.35%	144	Consumer Cyclicals
MCEM	The Monarch Cement Co.	10.00%	25	Non-Energy Materials
PEBK	Peoples Bancorp of North Carolina, Inc.	-2.22%	67	Finance
PSX	Phillips 66	16.21%	151	Energy
THFF	First Financial Corp. (Indiana)	0.33%	129	Finance
UNM	Unum Group	31.73%	399	Finance

Risk-O-Meter: **"red zone." Action: none. I continue to favor small-cap stocks in my taxable account.**



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Opinions are like Assholes…

Everyone has one…

It's especially true that (nearly) everyone has an opinion regarding the future direction of interest rates.

Except me.

I have no clue. I don't need to have a clue.

No one can predict where rates will go. Heck, the folks at the Federal Reserve who vote on the level of rates have no idea where rates are going. Last week, Jamie Dimon, the CEO of JPMorgan Chase, warned that we should be prepared for 7% interest rates. The market is betting that the end of rate hikes is near.

The market is factoring in rate *cuts* in 2024 amid a "soft landing" scenario for the economy (there's never a soft landing).

When will those rates be cut?

Here's a sampling of expert opinions on when from *Insider*:

- As soon as year-end, according to Bob Michele, the CIO of J.P. Morgan Asset Management
- February 2024, according to Preston Caldwell, a Morningstar Senior U.S. economist.
- Not before April 2024, according to David Einhorn, a well known hedge fund manager.
- May 2024, according to KPMG Chief U.S. Economist Diane Swonk.
- Between April and June 2024, according to the consensus of a Reuters poll.
- Second quarter 2024, according to Goldman Sachs Chief U.S. Economist David Mericle.
- Between May and end of 2024, according to Simona Mocuta, the chief economist of State Street Global Advisors.
- The second half of 2024, according to Vanguard's global economics and markets team.

Reading through the list of predictions above is downright exhausting. In reality, *no one knows*. The great thing is *we don't need to know* where rates are going. Instead, we can *react* to rate changes. When interest rates get cut, there will be *plenty of time* to respond. At first, it will seem like there is *no* time to react. However, just like how Rome wasn't built in a day, neither are bear or bull markets.

There will be a lot of volatility when the direction of interest rates changes. However, the Federal Reserve does not cut rates in one meeting only to raise them the next.

That's *not* going to happen.

Therefore, a new trend will form in interest rates and the financial markets. All we have to do is be patient enough to sit back and *let* it happen. Meanwhile, you can save yourself a lot of stress by ignoring all the bloviating and predictions about interest rates, because their guess is as good as yours.

What's more concerning about where rates are going is the level of freaking out at the *current* level of interest rates. Interest rates are at roughly normal levels. It's not like we are at 15%! *Artificially low interest rates* for years created many imbalances that will lead to significant ass-kickings.

First, trillions of dollars in commercial real estate debt are set to roll. It's going to be a bloodbath. Commercial property owners may leave the keys in the mailbox and let the lenders deal with the shit show.

The equity markets might be in for a good thumping, because *the* key driver of stock returns since the financial crisis 15 years ago has been stock buybacks. Companies aggressively issued debt to buy back stock. This financial engineering scheme boosted earnings per share while removing stock from the market.

Demand > Supply = Stock goes up.

That game is over. Companies can no longer issue cheap debt to buy back stock. Meanwhile, profit margins can only expand so much.

As profit margins revert to the mean in a more challenging economic environment and there are fewer financial levers to pull to generate earnings per share, the equation looks like this:

Supply > Demand = Stock goes down

There are zillions of dollars of capital dependent on artificially low interest rates. Now things might get painful as the economy and markets adjust. The pain felt wouldn't be so bad if that capital weren't levered up the wazoo. Leverage works until it doesn't. Then the piper's gotta get paid!

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