

**BEDELL FRAZIER**

INVESTMENT COUNSELLING, LLC

A BLUESPRING WEALTH PARTNER

FALL 2024

# Buckle Up for November

QUARTERLY NEWSLETTER

October 2024

# Buckle Up for November

2024 was guaranteed to be an eventful year. Of course, attention naturally gravitated towards the first Tuesday in November. And here we are, just a month out. The Presidential election is near. The visibility on victory is anything but clear. The implications are massive.



Politics and election cycles are never the primary driver for the Market. But they sure do influence. More important are earnings and economic cycles. James Carville made it clear what matters most to the American people when they head to the ballots. It's the Economy, stupid. He said that in 1992. He also asserted the Bond Market can intimidate anyone. Both still hold true today.



By Michael G. Frazier

## Inflation Tamed?

America's Economy has been chugging along all year. Calls for recession have proved wrong. Perhaps they're just early. Consumers have absorbed multi-decade high inflation but still had the travel bug with strong demand for activities and adventures. A strong Dollar went far overseas. The post-Covid World brought a surge in spending. The American people have shown an insatiable thirst for experiences and an economic resiliency like few others.

The Fed officially put an end to its restrictive monetary policy. The central bank cut interest rates for the first time since March of 2020. That was back deep in the heart of Covid. After a strong recovery for both the Economy and asset prices, the Federal Reserve launched a hiking campaign, raising rates 11 times, starting in the Spring of 2022. They took the overnight rate from zero to 5%+. That's where they stayed for 14 months. It was designed to choke off the multi-decade high inflation that sprung. The Fed has now declared victory. We're not so sure. More on that later.

## Buying Power

Interest rates hit multi-decade highs for we Americans. As inflation has eaten away at pricing power, consumers have leveraged credit cards to cover expenses. The American consumer is getting squeezed. Since 2019, price inflation is up nearly 30% cumulatively. We see it at restaurants, at the store, pretty much everywhere. The majority of Americans live paycheck to paycheck. Inflation crushes buying power.

The pressure has taken a toll. There's now well over \$1 Trillion in credit card debt. That translates to an average of \$6K per household. Borrowing with a credit card is both easy and costly. Interest rates on credit cards average 21%. It's an absolute crusher. Lower rates will help, but it's still dangerously high.

## There's No Such Thing as Free

The fact is, for 2 decades, Americans got really used to low rates and cheap money. We hadn't had inflation for a long time. Zero-interest loans were pervasive in our society. That is not normal. But many Americans didn't know any difference. Normalization has been bumpy. So, the Fed is calling this new stage "recalibration." That means higher rates for longer. That means higher costs. Years later, we are still paying the price for the Financial Crisis and Covid. Whatever it takes comes with a cost. We mustn't ever forget, there's no such thing as free.

Bonds stayed firm into the Fall, as they had already priced in the Fed cut. In fact, curiously, yields actually rose in the belly of the curve while the Fed reduced interest rates upfront. Commodities exploded higher. Crypto did too. The response was risk-on.

Perhaps most interesting was the Dollar. It fell. Importantly, the Dollar

weakness triggered a commodity price recovery that could stoke inflation again. When the Dollar goes down, things priced in Dollars tend to go up. That's a risk the Fed needs to worry about.

## Geopolitics – Ignoring the Risks

Wars in Ukraine and the Middle East have not had the negative impact on the Market that one might think. The Stock Market has largely ignored the risk, believing the issues would be contained within the regions and not have a material impact on the Global Economy and Corporate Earnings. Beyond all else, it's earnings that drive stock prices.

Military activity keeps expanding throughout Gaza and Israel and into Lebanon. The price of Oil is up as the fighting expands. WTI is still only in the low \$70s. This, despite a seemingly inevitable Israeli response to an Iranian attack. A large war premium is not yet fully priced in Oil.





## War Premiums

The US and Europe continue to urge a measured response from Israel that avoids Iran's nuclear facilities. An attack against Iranian Oil facilities remains a real possibility. Oil markets are pricing in some risk premium. But it's definitely not yet pricing in a fundamental disruption.

A spiraling Mideast conflict is a major risk. The Market has stayed surprisingly calm. An Israeli response looks likely after the Jewish holiday of Rosh Hashanah. It could very well happen around the ominous anniversary of the horrific attacks on October 7th. The Market is paying attention.

## China: Zero-Covid = Slow Growth

China has been facing a prolonged economic weakness. While the rest of the World has been dealing with hyperinflation, China's had the opposite: Deflation. The implosion of its housing market has dragged down its whole Economy.

China has yet to recover from Covid. Its Zero-Covid policy slowed economic activity and decimated the ability of consumers to spend. A strong post-pandemic bounce has never materialized. The Chinese people are struggling. Worries are high around job security as attention had been directed on exports given the weaker domestic Economy.

You name the economic measurement, China's been weak. Industrial production, Retail sales, Housing; They've all been sluggish. The Chinese Stock Market entered September at its lowest levels since 2019. Read that again. Lowest since 2019. The rest of the World has experienced great prosperity for investors. Not so in China.

To combat the slowdown, the Chinese government had been focusing its attention on supporting manufacturers.



Exports surged, which has not helped the Chinese consumer. What's more, it has irritated foreign countries, as domestic products can't compete. The Chinese subsidies skew the free market. That's why tariffs have become more popular in America and beyond. It's absolutely an issue in the Presidential election.

China's inability to address its housing crisis keeps hurting its people. The unemployment rate for 18-25 year olds was over 20%, before the government stopped reporting it. Beijing seems more focused on its global stature and winning the Digital Age. Big investments in automation and electric vehicles are paying dividends. But the benefits haven't been reaching the Chinese people.

## China Finally Playing Offense

China launched an aggressive interest rate cut campaign of its own to end September. The timing of the monetary stimulus package, aimed at restoring confidence, may help China approach its full-year growth target of "around 5%". Growth has been anemic.

The US Federal Reserve's aggressive cut gave the People's Bank of China room to ease in the face of deflationary pressure. It had likely been hesitant prior, as higher

American interest rates generally weaken foreign currencies. Going at easing alone, China could have triggered a massive capital flight to the US. It looks like the Chinese government saw a window and must have decided this is their "whatever it takes" moment. With a population of 1+ Billion and the second largest Economy on the planet, what matters most is the Chinese consumer.

Chinese stocks soared on the news, taking other foreign markets with it, which have drastically underperformed the US for years. You know what else took off? Commodities. China is a large importer of commodities and if its Economy is starting to turn around that will increase demand for Oil, Copper, Agriculture and various other basic materials. Copper prices jumped on a China stimulus package. That also could trigger a return to inflation. That's something the Market and the Fed need to be watching closely.





## Japan Woke Things Up

Remember the Market crash in Japan in August? It still hasn't been fully resolved. The Japanese Central Bank raised interest rates for the first time in over a decade. It sent the Yen currency surging and Japanese stocks sinking. It caused a global sell-off. The Dollar plummeted. The Bank of Japan immediately threw caution back to the Market to stabilize the situation. It worked. There's also a new leader running Japan.

The Yen has been under pressure again after dovish comments from Japan's newly elected Prime Minister. The central bank is seemingly re-thinking another interest rate hike anytime soon. The Yen-carry-trade has been in place for nearly 2 decades. The unwind contributed to the Global Market meltdown. It is again regaining momentum as traders are betting the Yen will weaken further. That sent both Japanese stocks and the US Dollar higher. One must be careful there.

## AI Still the Driver

The secular growth theme of Artificial Intelligence has been the undeniable engine for the Stock Market in 2024. Tech has been a standout leader. Massive investment spending has brought a swelling of revenue and earnings growth into semiconductors

and storage providers. Those with the deepest pockets are best positioned. The Tech Titans still reign supreme. Their stock prices reflected it heading into Summer.

The good news for the overall health of the Stock Market has been the rotation of leadership. The concentration in Tech has been broken up. A correction triggered flows into other areas that had previously not participated. There's been a great deal of activity below the surface while the S&P 500 kept reaching new highs. AI is clearly where the growth is. But corrections always prove an important lesson: Price matters. It got a little euphoric there.

## Powering AI

America is hitting an energy bottleneck as the AI revolution is accelerating power demand to unprecedented levels. Data centers supporting the computing power are popping up all over the country, which has created a need for clean and sustainable sources of energy such as nuclear power. The ability to power them is getting stretched. America is struggling to power the Digital Age.

Modernizing our "electric highway" by adding new capacity will enable new companies and new energy sources access to the grid. Competition will raise the bar. This will provide consumers more choices, which should, in turn, increase quality of

service and lower power prices. Better forecasting and more efficient management will enhance production. AI is proving to increase both demand and solutions for America's energy needs.

## Back to the Future – Nuclear

Something happened in September that sent the Energy Industry buzzing. Microsoft announced a partnership with Constellation Energy to revive 3 Mile Island. Microsoft will purchase the carbon-free energy produced from the Pennsylvania plant to power its data centers to support artificial intelligence.

Demand for clean, reliable and cost-effective energy has never been greater. Nuclear is able to stay on at all times of the day and night, unlike wind and solar. The subject of energy always brings controversy. That won't go away any time soon. But new sources are needed while demand grows. It's very investable.

## Still a Crude World

Despite all the advancements and innovation, the World still runs on Crude. That has been abundantly clear since Covid and the war in Ukraine. Supply disruptions nearly crippled the Global Economy once demand picked back up.

The US is currently producing at a record pace of over 13 Million barrels of Crude per day. That is substantially more than any country, including Saudi Arabia. The output growth has helped tame gas prices and, perhaps more importantly, undermined the influence of OPEC and Russia following its invasion of Ukraine in 2022. This has clashed with the Biden administration's clean energy agenda, though for the time being, inflation concerns, and energy independence leaped to the top of the priority list.

Despite two major ongoing wars, Geopolitics have failed to generate any significant reaction to Oil prices. It goes to show how well supplied the



Market is. Besides, some nations, like China and India, are importing Crude from shadow fleets, mostly Iranian and Russian. The production cuts and subsequent roadmap from Saudi Arabia bought some political goodwill in Washington by helping the US craft a more comprehensive energy policy, which it lacks. The time is far past due to come up with a long-term, comprehensive energy policy for America. That will be extraordinarily investable.

## Security and Defense

It's a complicated and dangerous world in which we live. Geopolitical tensions, military activity and cyber theft are back on the rise. Defense and Cybersecurity budgets are expanding in both the corporate World and governments. Sophisticated solutions are essential to compete and protect. Defense and cybersecurity companies are well-positioned in this environment. We continue to be invested there.

## Back to the Election

There's great uncertainty as to the outcome in this run for the White House in 2024. The year began with what seemed like a predictable matchup. That quickly changed. An assassination attempt against former President Trump and a concerning debate performance from President Biden changed everything. Trump's popularity soared while Biden's soured. Then, Vice President Harris's hat got thrown in the ring. That injected energy and gobs of money into the Democrats' campaign. Both sides are running heated campaigns. By all indications, it's going to be a razor-thin result.

The Economy is the top issue for the American people. This is no surprise; People tend to vote with their wallets. 2 in 3 voters say the country is on the wrong track. Consumer spending accounts for 70% of economic activity. US GDP grew 2.8% in Q2 and is estimated to have grown close to 3% in Q3 when the results are reported later this month. But the American people aren't feeling the prosperity.



Despite the solid economic growth and the Stock Market at all-time highs, the average American keeps struggling to get ahead. Inflation is a big reason. Prices are high everywhere. Life is really expensive. Donald Trump has consistently polled better on handling the Economy, but that lead has been shrinking of late. This is such a critical issue as the American people head to the ballot box. Carville said it best: "It's the Economy, stupid."

## Record Campaign Spending

From Labor Day thru the election, Americans will not be able to escape the political campaigns. \$170 Million will be spent on television ads. Traditional TV ad spending is expected to increase 7.5% from the 2020 election. But the growth is going to be explosive in digital ads, increasing by over 150%. For the first time, digital ads will outspend TV at \$200 Million.

Streaming/connected TV ad spending is expected to increase by a whopping 500%. Apple, Amazon and Netflix say they won't accept political ads. They can afford not to. But local TV stations depend on the revenue, so get ready to be inundated if you watch local news. Cable news is ground zero for ads. Swing states will be bombarded.

There are seemingly seven states that

will determine the outcome. Money is pouring into them. Pennsylvania is receiving the most. \$190 Million is being spent in the Keystone State. That is double the next largest state. In case you're wondering, Michigan is that state. Money talks big in election years.

## Tax-Cuts on the Table

The 2017 tax cuts are set to expire at the end of 2025. The Congressional Budget Office estimates that extending the individual tax cuts would cost \$4.6 Trillion over the next 10 years. Neither party wants to raise taxes on all Americans. According to our Washington sources, it seems likely that Congress will extend the current rates for most tax brackets, except for the top bracket. That would help mitigate the cost of the extensions.





Kamala Harris indicated a plan to raise the corporate tax rate from its current 21% to 28%. Donald Trump has said he wants to lower it to 15%. Our Washington sources believe neither will happen. If Harris wins, it's doubtful Congress will raise the corporate tax to 28%. But a small increase to the 23-25% range is possible. If Trump wins, they believe it is highly unlikely Congress would cut the corporate rate to 15%. In fact, Congress could even raise the rate as a way to pay for the extension of lower individual income tax cuts. Populist Congressional Republicans are unlikely to fight for lower corporate income tax rate. In fact, some would even support a small increase.

The Market cares about capital gains. The current Federal capital gains rate is either 0%, 15% or 20%, depending on your income. It is believed that if re-elected, Donald Trump would keep them as is. Kamala Harris has proposed an unrealized capital gain tax for taxpayers with net wealth above \$10 Million, a 28% capital gains tax rate for taxpayers earning more than \$1 Million per year, and an increase in the net investment income tax to 5% from 3.8% on wealthier taxpayers. Our Washington sources believe there is next to no chance of these being embraced, even in a Democratic sweep. Importantly, Democrats had a chance to pass a higher capital gains tax when they controlled Congress in 2021-22 and

failed to do so. You know how it goes, politicians tend to politic.

## Fiscal Discipline Lacking

America has a spending problem. The United States has accumulated over \$35 Trillion in debt. That's over \$100K per citizen. It's never been close to that high before. It costs over \$1 Trillion per year just to service it. Neither political party has demonstrated a plan, nor a desire, to address it. This cannot last forever.

The Bond Market has been somewhat tolerant of the excess spending over the years. But now that rates are higher and the debt levels are climbing, it is increasingly clear that patience is running out. The long-end of the yield curve is very vulnerable with deficit increases and no debt reduction plans. That could send long-dated Treasury yields skyward and the Dollar falling. When it wants to, the Bond Market has proven it can intimidate anyone.

## More Gridlock?

Our sources believe, entering October, that the Democrats are likely to flip the House and Republicans are likely to take back the Senate. That would provide more gridlock, which the Market often likes. No major changes or surprises. Of course, all of this could change in an instant. A divided Congress would make it difficult for the

new President to pass their economic agenda.

Tariffs are likely, regardless of who wins. Donald Trump has said he would slap a 60% tariff on Chinese imports and 20% on goods from everywhere else. Kamala Harris hasn't specified what she would do here, but the Biden-Harris administration maintained the Trump tariffs from 2019. Populism is on the rise around the globe. There's really no such thing as free and fair trade right now.

There is reason to believe the election outcome won't be immediately known after November 5th. What's more, a case can be made that neither side will accept the result. That adds a layer of risk to what is normally the start of a seasonally strong period. The Market hates uncertainty. It hasn't seemed too concerned about the election uncertainty. We believe that changes in October.

## October Surprise?

An escalation of war will reverberate far beyond the Middle East. Being just a month out from the election, it could be the "October Surprise" that shakes the Presidential race. We shall soon see. Allies and adversaries alike are jockeying for position with eyes wide open. They have to prepare for either outcome. America's Presidential election is that big. Gold continuing to hit new, all-time highs speaks to the risks and uncertainty ahead.

## No September Swoon

September didn't bring the typical swoon this year. The combination of Fed easing, and expectations of a soft landing has kept the Stock Market buoyant. September has historically been the worst month for stocks. The S&P had never hit an all-time high in the month of September. It did this year. The uptrend has continued with 10 monthly increases in the last 11. April was the only decliner. The Market has had every reason to go down in 2024. And it hasn't.





Stocks sure celebrated the Fed move. The Dow and S&P both hit fresh, all-time highs. There's nothing bearish about that. That said, the first rate cut historically has not been bullish for stocks. The reason is rate cuts generally come in response to already present economic weakness. The ensuing 3 months tend to be choppy, with a downward bias before settling in.

There are some areas that have historically worked though. Both Health Care and Gold have done well when the Fed started cutting rates. Utilities and other dividend stocks have done well too. On the flip-side, Tech and specifically Semiconductors, have historically been big losers after the first cut. We've been seeing this type of rotative price action already and are positioned accordingly.

## Earnings Season

It's that time of year again. October brings Corporate America's Q3 report card. The Street estimates S&P 500 earnings grew 4.6% in the September quarter. This estimate is down from the +7.8% expected at the start of Q3 and the +11.3% actual for Q2. Tech, Health Care and Communications Services are expected to deliver double-digit earnings growth for Q3, while Energy is expected to see a double-digit contraction.

The big keep getting bigger. The six largest companies are expected to grow earnings 16.3% in Q3. They're the Tech Titans. The rest of the S&P 494 is expected to grow by just 1.5%. Then the growth is expected to accelerate. For Q4, the Street expects these Titans to grow a combined average of 18.3% while the rest of the S&P grows just under 9%. The acceleration is expected to continue. The Street expects earnings to grow another 15% in 2025.

## Buckle Up for November

The likelihood of another 1/2-point cut from the Fed seems to be shrinking. The Economy is still chugging along. The Job Market is slowing. Earnings will be an important tell. Expectations are already high with the S&P trading well north of 20x estimated earnings. That's expensive by most measures. But demand for stocks has been strong all year. Buy the dip keeps working. It's going to work until it doesn't.

Over the past 6 Presidential cycles, the Stock Market has performed well, with some speed bumps leading up to November. What's encouraging is the post-election trading has seen strong overall returns and cyclical outperformance. Q4 is always seasonally the strongest. November and December have averaged 4.2% gains in this century. Getting there is the challenge.

With so much of the positives already priced in, the risk/reward for the near-term seems unbalanced. We expect increased volatility with a downward bias until some of the risks are either minimized or eliminated. That seems unlikely for now. Earnings Season and the election will be Market moving. Geopolitics will be too. We're starting to play a little more defense until things clear up and the corrective price action runs its course. So, buckle up and hang on tight. We see more turbulence ahead before smoother air returns.



To view past Quarterly  
Newsletters,  
visit our website at:

*BedellFrazier.com*

# BEDELL FRAZIER

INVESTMENT COUNSELLING, LLC

A BLUESPRING WEALTH PARTNER

