ANDINA
ADVISORS

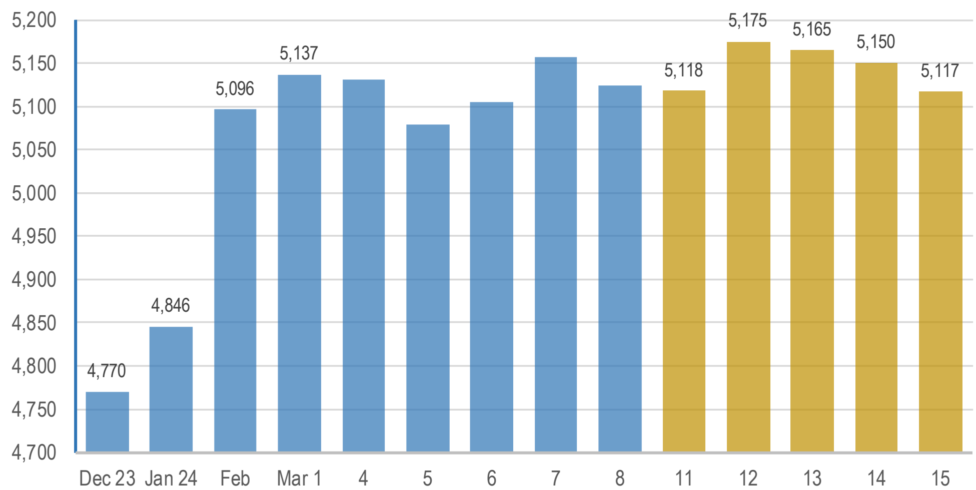
Piano Man

Weekender

March 16, 2024

Good morning and welcome to the *Weekender* for Saturday, March 16, 2024. It was a slightly negative week for both equity and debt markets. Equities measured by the S&P 500 were lower by -0.13%. For March, equity markets have been marching sideways. With stickier inflation, interest rates have been adjusting higher, putting downward pressure on bond prices.

S&P 500 Index Levels
(Source: Bloomberg)



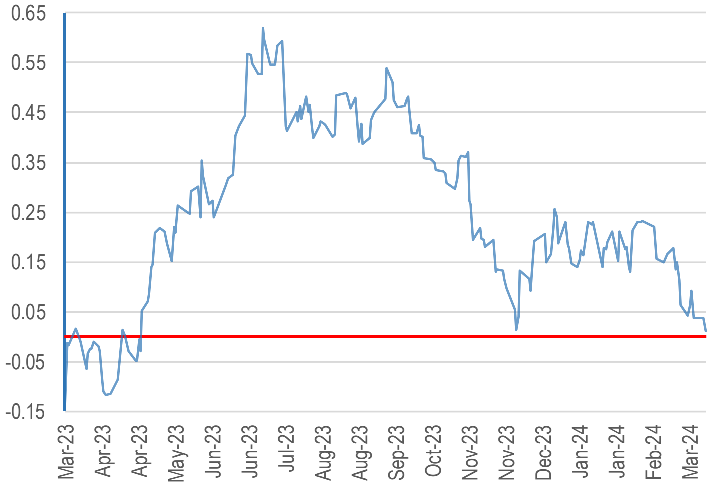
One Friday each quarter is known as a triple witching. When stock derivatives, options, and futures expire on the same day, this usually results in more volatility than is typical on the day and the week preceding. Because of triple witching, it isn't easy to draw too much of an inference from market movements. But even without the witches, last week's data sent several confusing signals.

Macroeconomic news suggests the US economy is resilient but slowing. Recent economic data has surprised economists and strategists but to the downside. Inflation is falling, but at a much slower pace than many expected. Softer economic data gives the Federal Reserve some justification for lowering rates from their restrictive levels, but stubborn inflation does the opposite. Last week, financial markets chose to focus on inflation, resulting in higher yields, lower bond prices, and sanguine stocks.

Bloomberg US Economic Surprise Index

March 15, 2023 - March 15, 2024

(Source: Bloomberg)



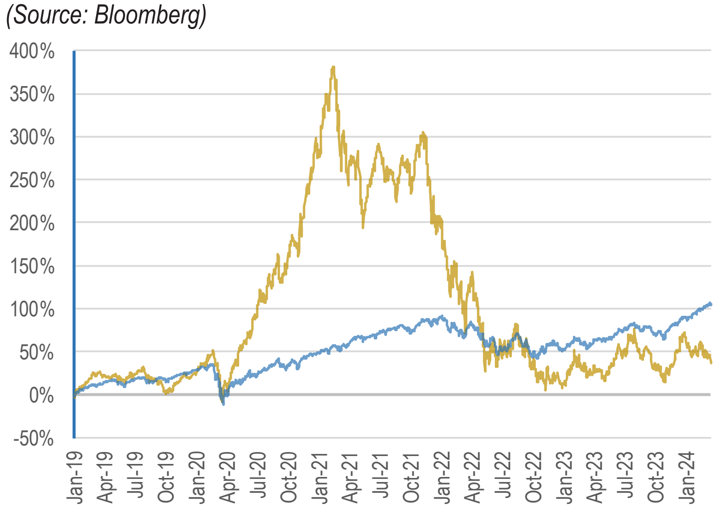
As most year-end targets for equity markets have already fallen to solid markets, economists and strategists have been raising their targets for major equity indices and boosting interest rate and inflation expectations. A reasonable glide path to the Fed's target of 2% inflation, which seemed granted a month ago, now looks uncertain. A bout of stagflation, where growth slows, and inflation remains, benefitting gold, commodities, crypto, and value, is as likely as unwelcome. More on that in a couple of weeks.

Pandemic-era financial markets in 2020 and 2021 were driven by trillions of dollars in found money leaking into every asset class, giving rise to myriad market dysfunctions.

Money Losing Tech (Gold) and S&P 500 (Blue) Cumulative Return

January 1, 2019 - March 15, 2024

(Source: Bloomberg)



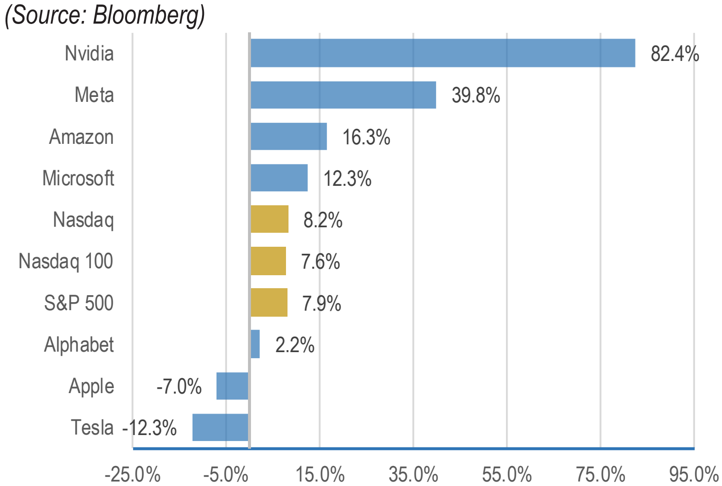
Money-losing concept stock valuations were unjustifiably propped up by a newly converted group of couch traders playing with government stimulus money while they "worked" from home. As the wave of pandemic-era excess recedes, non-profitable technology punters have fallen back to where they started before the pandemic.

Equity markets going nowhere in March have been chiefly a function of a raft of conflicting economic data. Equity gains for the S&P 500 of 24.2% in 2023 were the providence of the magnificent seven (Tesla, Apple, Alphabet, Microsoft, Amazon, Meta, and Nvidia), most of which held a perceived leadership role in the future of artificial intelligence (AI). Because of their relative size, they disproportionately impact the equity indices in which they are components. In 2024, the year-to-date gain of the Magnificent Seven is 13.2%.

Year-to-Date Returns

January 1 - March 15, 2024

(Source: Bloomberg)

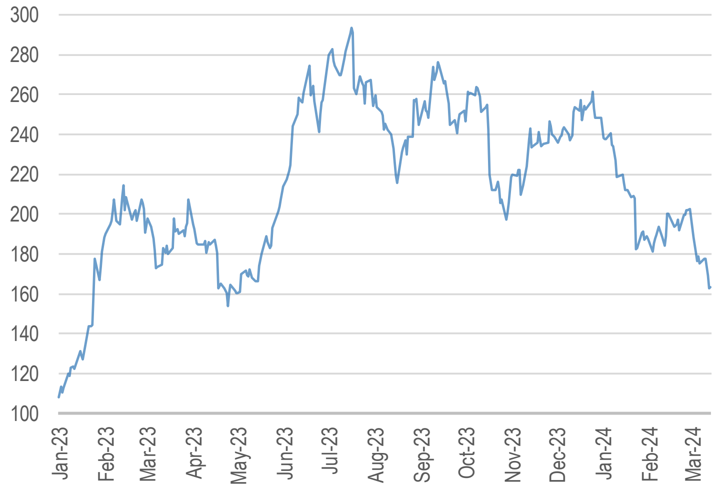


Less magnificent members of the Mag 7—Apple and Tesla—are lower on a year-to-date basis due mainly to unique company characteristics. Demand for Apple iPhones is softening, especially in China, due to economic stress in the Middle Kingdom and a structural shift among Chinese consumers' preference for local instead of American brands. Tesla is having a horrible, no good, very bad year. Consumer sentiment regarding electric vehicles has been a buzzkill over the past year. A general lack of "cool" translates into softer Tesla unit demand. Price discounts have also become common, cooling the secondary market for used Tesla cars. Meanwhile, Chinese-made EVs are getting better made, priced, and appreciated. Seems like Tesla is just a car company, after all. And to our mind, it is still an expensive one.

Tesla Stock Daily Levels

January 3, 2023 - March 15, 2024

(Source: Bloomberg)

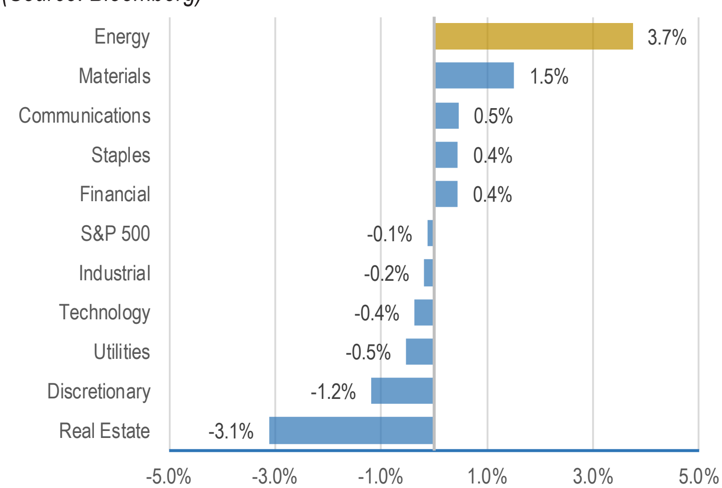


Oil and energy outperformed all other sectors last week due to higher crude prices and a new report by the International Energy Agency forecasting a global crude oil supply deficit this year. In their analysis, crude inventories are expected to shrink, and OPEC+ will hold on to tight supply for the rest of 2024. With a strong economy in the US, recovery in Asia, and perpetual malaise in Europe, the outlook for demand is much better than it was only a couple of months ago.

Last Week Sector Returns

March 8 - 15, 2024

(Source: Bloomberg)

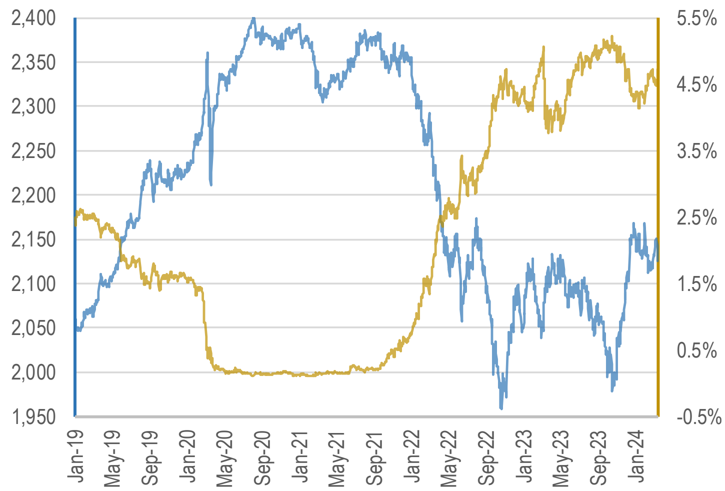


The Bloomberg Aggregate US Bond index has been running silent for the past few weeks. However, this week, it was down -1.2% as stiffer inflation expectations dashed hopes of some traders and investors that the Fed would be dropping interest rates soon. While no rate move is expected at the Fed's meeting next week, they will likely adjust their rate view, leaning toward fewer rate cuts this year. Economic data from this week suggest that the higher for longer mantra will persist through most of 2024. That is unless something, like the labor market, breaks. But that seems unlikely in the near term.

Bloomberg Aggregate Bond Index (Blue) and US Government 2-Year Bond Yield (Gold)

January 1, 2019 - March 15, 2024

(Source: Bloomberg)

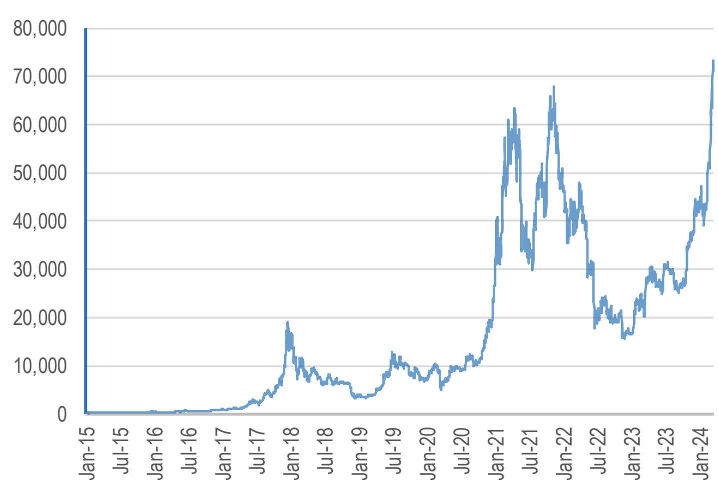


Among alternative financial instruments, king to Bitcoin for the week and all of 2024. No valuation metric justifies recent moves or any particular price level. Renewed interest from the beginning of the year comes from the Securities and Exchange Commission's recent approval of cryptocurrency exchange-traded funds. A general "risk on" mood also plays a role, as crypto is the poster child for investment risk. By the end of 2024, the US government is expected to release details of its digital dollar initiative, which will be a formidable transaction alternative to existing cryptocurrencies. A puny

Bitcoin Daily Price

January 1, 2015 - March 15, 2024

(Source: Bloomberg)



fraction of traded cryptocurrencies is used as a transactional currency. Hype and fear of missing out (FOMO) drive demand and pricing. Last week, Buffett reaffirmed that crypto is 'rat poison' and professed 'with certainty that they will come to a bad ending.' Conservative as we are, we align more with his view.

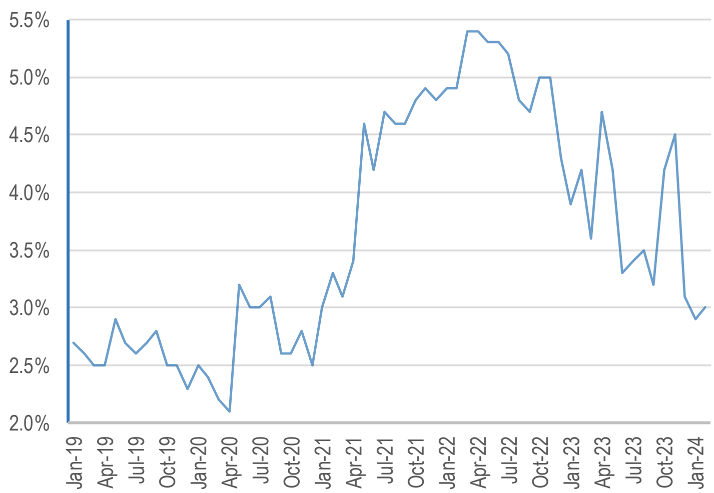
Economic Summary

Inflation data, including consumer, producer, import, and export prices, was released this week. All the data showed stubborn resistance. While the inflation rate is well off the highs from 2022, the prospect of getting the rate of inflation close to the Federal Reserve's target of 2.0% is looking remote in 2024. As we have mentioned numerous times, the last mile of the fight against inflation will be hard fought. Consumers expect inflation to be approximately 3.0% a year still ahead. The "higher for longer" interest rate mantra is directly tied to stubborn inflation expectations. Even so, we do not expect rates to stay at their current level.

One-Year Consumer Inflation Expectations

January 1, 2019 - March 15, 2024

(Source: Bloomberg)

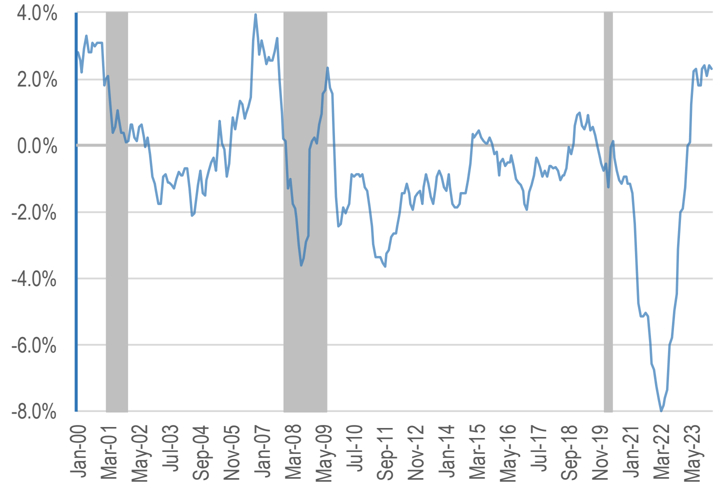


We believe the Fed's target interest rate at 5.5% is economically restrictive, although not enough to tip the economy into recession. As more evidence of softening demand manifests, the Fed can lower rates while keeping them in restrictive territory. Residential mortgage demand has fallen to levels not seen since the 1980s. A large part of the drop comes from equity withdrawal refinancings, which have gone from plentiful during the low rates of the pandemic to endangered today. Its spread above the inflation rate is 2.3%, which, in historical terms, is very restrictive. By the same metric, interest rates were more restrictive before the internet bubble recession and the credit crisis.

Fed Rate Adjusted for Inflation

January 2000 - March 2024

(Source: Bloomberg)



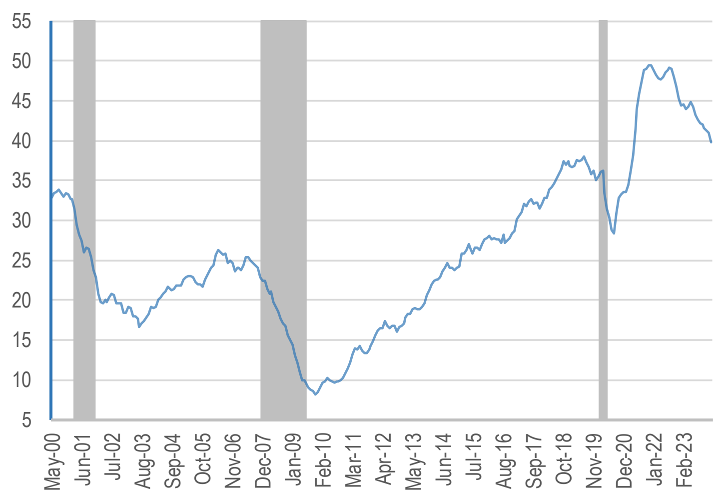
In the face of restrictive credit, the economy continues to exceed most economists' expectations. The Atlanta Fed GDP Now data estimates that the first quarter of US economic growth will be approximately 2.5%, a respectable and non-recessionary figure, one of the most restrictive in recent economic history.

Economists often discuss the long and variable lags that follow monetary and fiscal policy changes. In candor, no one knows when the full effects of pandemic stimulus will end or when the full restrictive power of higher rates will be fully felt. Some data suggest that things are getting closer to their pre-pandemic normal. For example, small businesses' assessment of whether difficulty hiring people is a prominent concern has fallen significantly and is now within the trend.

Hard to Hire Index

May 2000 - February 2024

(Source: Bloomberg)

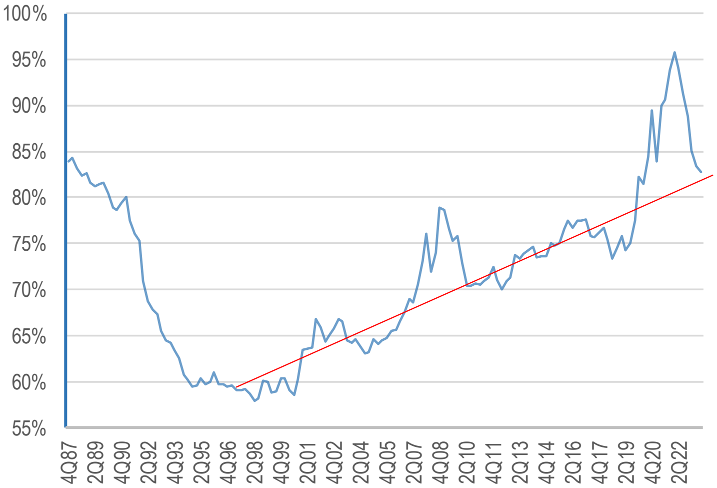


Cumulative household savings, which includes total holding of checking and savings deposits and money market investments, has come down significantly, suggesting the consumer has blown a lot of their dry spending powder. Consumers save almost nothing on each marginal dollar earned while consumer credit is at all-time highs. We believe stimulating the consumer before the pandemic continues to support consumer spending on services and products. As savings continue to erode and credit becomes increasingly heavy, the consumer will begin to pull back.

Cumulative Household Savings Percent of Disposable Income

1987 - 2023

(Source: Bloomberg)

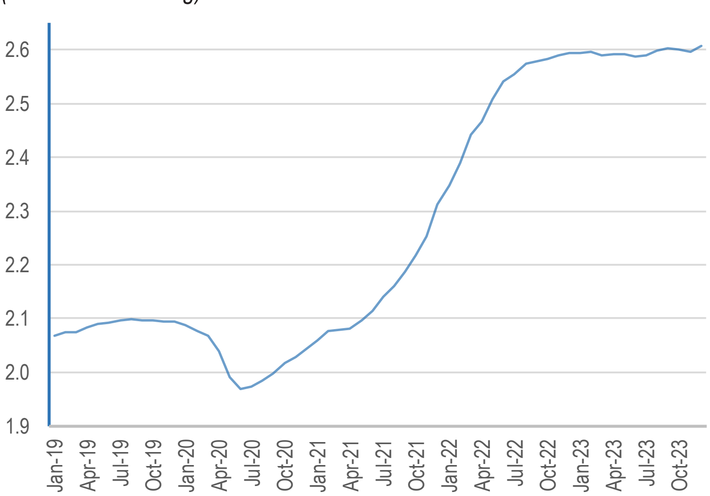


Inventories rose to record levels during the pandemic's frenzy of stressed supply chains. We expected a well-endowed consumer to spend enough to pull inventories down to more normal levels eventually. That has not happened. Business inventories continue to hover at record levels. We

US Business Inventories

May 2000 - February 2024

(Source: Bloomberg)



believe that as consumer demand softens, businesses must sluff off excess inventories, especially as holiday products arrive at the end of summer. Discounts will lead to slender margins and reduced profit expectations.

One More Thing

One more thing. On a recent business trip to India, a Cambodia side trip was organized to visit an orphanage where our family made very modest contributions. While I consider myself travel savvy, having spent twenty years in international finance traveling to most parts of the world, nothing prepared me for the full-on assault on the senses that is India. As this largest democracy rises from bracing poverty, it will shake the planet in profound and unpredictable ways.

While poverty levels were similar between Cambodia and India, some differences spoke volumes but were rarely spoken. In Cambodia, a general sense of cleanliness was emblematic of Cambodians with meager means compared to the wrenching conditions of India's destitute. As I spent time among them, I was taken by the hope in Cambodia's rising generation. On a Sunday, I observed a youngish church congregation listening and taking notes as they listened to visiting representatives. In the brutality of Cambodia's Khmer Rouge period, anyone with education and a desire for learning was rounded up and re-educated or executed. Surviving generations still tend to eschew any pretense, like education or religious meetings, that may make them stand out.

After worship, the small orphanage offered a tour. It was magical, and I quickly fell in love with every child, especially Chen, a seven-year-old boy. Most of them had been turned over by their parents because they could no longer bear the burden of raising them. I listened to their English, math, and history classes as the children sat in rapt attention until it was time for their music lessons. As the students gathered around the teacher, she sat down, slid open a drawer, removed a manila file folder, opened it, and laid it on the table. An outline of a piano's white and black notes was sketched on the open folder. As her fingers moved across the notes, she mouthed the sounds of each note and talked about the keys, notes, timing, and melody.

The contrast between the dirt floor of the orphanage and my suite at the five-star Raffles Hotel was shattering. As I returned, I cornered the concierge and organized a feast in a private dining space for the kids and staff of the orphanage.

They all arrived around noon the next day. As they walked in, their eyes grew to the size of tea saucers. We had a wonderful meal together and adjourned to the hotel bar, which was largely empty except for some more persistent patrons. The oldest child saw a stand-up grand piano against a wall and asked me for approval. As we surrounded the piano, he began to play, transferring his file folder practice to the sweetest melodies. Without clamor, each of the children waited longingly for their turn. My heart was whole, and I did not want the evening to end. Ever.

Cicero said, “Gratitude is not only the greatest of virtues but the parent of all the others.” I was, for at least a moment, bursting with gratitude. Not because, by comparison with their material lack, I lived a life of extreme abundance, but because, in the scarcity of their lives, they had become like he whom I most wanted to emulate. Several life events have recently reinforced the power of gratitude and how it bounds the value of our lives.

Jeanne, Rebekah, and I have discovered a new mantra based on a poem attributed to clergyman William Henry Channing. Channing served as the chaplain of the US Congress, among other positions. His close friends were Susan B. Anthony, Henry David Thoreau, and Ralph Waldo Emerson.

My Symphony

William Henry Channing

To live content with small means.
To seek elegance rather than luxury, and refinement rather than fashion.
To be worthy not respectable, and wealthy not rich.
To study hard, think quietly, talk gently, act frankly, to listen to stars, birds, babes, and sages with open heart, to bear all cheerfully, do all bravely, await occasions, hurry never.
In a word, to let the spiritual, unbidden and unconscious grow up through the common.
This is to be my symphony.

Conclusion

That’s it for this *Weekender.* We want to add a section to future *Weekenders* that includes answers to your questions. If you have something you would like addressed, please email me at carywasden@yahoo.com. Have a grateful week.

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