RESEARCH CAPITAL CORPORATION

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The market has rallied strongly lately. It climbed 6% in July.

The mainstream media does an excellent job of reporting all the things that are wrong with the world each day. Reporters spend little or no time on what is going right. Take inflation, for example. It recently hit the highest level in almost 41 years.
Not good.

You’ve heard and seen plenty about high food and fuel prices. Inflation hurts the consumer and eats into the profits of small-business owners. The U.S. Federal Reserve might push the U.S. economy into a recession by jacking up short-term interest rates to combat high prices.

All true. But it’s not the whole story.

Financial markets - which represent the buying and selling decisions of the best-connected people on the planet - are forward-looking. They tell us what likely lies ahead. Right now, markets are shouting loud and clear that prices have peaked and are quite likely about to come down.

The Bloomberg Commodity Index is down 18% from its June peak. Crude oil has fallen 22%. (You've already seen the effect at the pump.) Copper is down 33%. Lumber is down 54%.

The U.S. dollar recently touched a 20-year high. (This is disinflationary as it makes U.S. exports more expensive and imports less expensive, keeping a lid on prices.)

Gold, the traditional inflation hedge, is down 5% in July and 7% for the year.
The yield on the U.S. 10-year Treasury is a measly 2.8%. (If bond investors believed high inflation was here to stay, yields would be much higher.) Even U.S. Treasury Inflation-Protected Securities - or TIPS - are down year to date.

Why would all this be if high inflation were likely to persist long-term or push higher still?

There is plenty of other good news that you rarely hear. U.S. Corporate profits jumped 11.4% in the first quarter. While second quarter profits are still coming in, companies that have reported have mostly beaten expectations. Analysts expect double-digit profit gains in the second and third quarters as well.

A quarterly survey of chief executives, conducted by the Business Roundtable, showed that CEOs remain positive. The Business Roundtable's CEO Economic Outlook Index - based on corporate leaders' outlooks for their companies' performance - clocked in at 95.6 in the second quarter. Anything above 50 indicates expansion. It was only 76.7 in the pre-pandemic fourth quarter of 2019.

This confidence is reflected in current labor conditions. The job market is drum tight with payrolls up a blistering 1.1 million over the past three months.

U.S. household income is near an all-time high. So is household wealth at $149.3 trillion. (Rising real estate prices have mostly offset declining stock and bond prices.)
And consumers are flush with cash, holding more than $2.5 trillion. I'm not arguing that everything is rosy in the world. That's not the case.

We still have global supply chain issues (although they get a little better each day), lockdowns in Asia, and a lingering conflict in Ukraine.

Yes, it's possible that the central bank could take interest rates too high too fast, pushing us into a recession. Some would say the inverted yield curve - short-term rates are now higher than longer-term rates - foretells exactly that.

But no recession in U.S. history has ever started with unemployment this low and hiring this strong.

The stock market has fallen this year because investors have priced in a shallow recession. But if a shallow recession is all we get - or if we avoid a recession altogether - share prices will most likely take a bounce from here.

And the move has the potential to see stocks move higher.

How are we preparing for this? By holding only recession-resistant companies with rising sales and earnings, excellent prospects, and substantial share repurchase plans.

That means we're playing it smart - and safe - with our current portfolio.

In short, stay the course and remain well positioned for potential future gains.

Respectfully,

John

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