Markets Reflect a ‘Snapshot in Time’ that Can Change Quickly

October generally served up more tricks than treats for investors, but the Federal Reserve helped make up for that as soon as the calendar flipped to November. The Fed’s dovish comments about short-term interest rates on November 1 gave a much-needed boost to the struggling markets. Although the boost came too late to be reflected in your latest financial statements, the Fed’s more cautious tone may bode well for investors for the rest of the year.

The Fed’s comments came at their November 1 meeting, where they announced they would keep their benchmark short-term rate unchanged for the second meeting in a row.[1] Although the news was expected, it still helped give Wall Street a boost after suffering its third month of losses. Both the S&P 500 and the Nasdaq finished October down by over 10%, putting them in correction territory[2], and the market overall remains down by more than 10% year-to-date. But following the Fed’s meeting, the S&P spiked by 5.85% and the Nasdaq jumped by 6.61%.[3] The bond market also rallied, triggering the most significant drop in long-term interest rates in months. The interest rate on the 10-year-government bond – which, between September 1 and October 31, had risen from 4.18% to 4.93% – dropped back down to 4.57% within two days of the Fed’s announcement.[4]

Most analysts believe the markets rallied because investors are cautiously optimistic that the Fed’s second pause in a row is a sign that they are done raising short-term rates altogether. While it is possible they have finally finished after more than a year-and-a-half of raising rates at a historically aggressive pace to fight inflation, Fed Chairman Jerome Powell did say further rate hikes may be considered in the coming months. It will, of course, depend on whether inflation keeps heading in the right direction, along with other economic indicators.

Portfolio Impacts

So, what did all this mean for your portfolios in October? Well, once again, October itself was another relatively tough one for the markets compared to the first half of the year. As noted, the trend of rising long-term interest rates that began back in August and continued through September continued once again in October. As a result, most investors saw their asset values drop to some degree. For those of you in our portfolios of bonds and bond-like instruments, your values, depending on your individual holdings, were down on average by about 3% when October ended – and that’s what you’ll see reflected in your latest statement. But here’s the good news: by the end of the second day of November, thanks to the Fed-induced rally I just discussed, most of those losses had already been recovered.

The point is that your statement each month represents a snapshot in time, and that snapshot can change dramatically from day to day, or even hour to hour. That’s especially true in a period when the Fed is actively manipulating interest rates and the markets are hanging on their every word. How long will this kind of volatility continue?

It’s difficult to say. While it’s true the Fed may be at or near the finish line, it’s also true that the full impact of their rate hikes has yet to be felt. The economy and the markets are still adjusting to higher

rates, and one of those adjustments is the reason investors have been facing headwinds again in recent months after getting a reprieve from them in the first half of the year.

The Yield Curve Issue

As I explained in last month's newsletter, long-term rates have been rising again despite the Fed's pausing of short-term rate hikes because the bond market is probably now convinced of something it had been skeptical about earlier this year: that the Fed is serious about trying to keep short-term rates at their current elevated level or higher for some time to come. That being the case, the bond market has been trying to bring long-term rates up to closer to short-term rates to correct the inverted yield curve.

As I've also explained many times, an inverted yield curve – in which short-term rates are higher than long-term rates – creates hardships for banks and is considered a warning sign of a recession. With the Fed's benchmark short-term rate now at about 5.4% and long-term rates still nearly a full percentage point lower (as of this writing), the U.S. yield curve remains inverted. As for how aggressive the bond market may get in trying to correct it remains to be seen.

The good news, again, is that the Fed is continuing to talk and act more conservatively. That gave the markets a welcome boost to start the month, and we may see that more optimistic trend continue. Either way, the bottom line – as I've said many times now – is that after one of the worst years in history for our portfolios (and investors in general) last year, we can at least continue to feel confident that the worst is over. A few months ago, our portfolios of bond and bond-like instruments were up by about 7% on the year. Although we gave a little of that back in recent months due to the issues I just discussed, as of early November we were back up by about 6% year-to-date – which is right on target with our goal. And, as I also always point out, these fluctuations in value are mostly irrelevant anyway when you're investing for income because your interest and dividend return are unaffected.

On that note, I also want to mention that if you notice something in your latest statement that seems to indicate that a particular interest payment went down last month, it is not accurate. It's merely the result of a clerical issue resulting from the way Schwab transferred all our account information from TD Ameritrade two months ago. We have coached them on how to fix it to make the information accurate, and hopefully, you will see this reflected in your next statement. As always, if you have any questions about this or any other matter, please give our office a call at any time.

1 "Federal Reserve Leaves Its Key Rate Unchanged," Associated Press, Nov. 1, 2023

2 October 2023 Review and Outlook, Nasdaq.com, Nov. 2, 2023

3 "Wall Street Flat After Fed Rally as Fed Speakers, Treasury Auctions Eyed," Reuters, Nov. 6

4 MarketWatch.com

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November 2023 Recipe: Honey Butter Roasted Carrots

Ingredients:

1 lb. carrots, tops trimmed, and skin peeled (two bunches of carrot tops)
2 tablespoons melted butter
2 cloves garlic, minced
Salt and freshly cracked black pepper to taste
2 teaspoons finely chopped parsley leaves
2 tablespoons honey or maple syrup or to taste

Instructions:

Preheat the oven to 400°F.

Toss the carrots with the melted butter, garlic, a large pinch of salt, black pepper, parsley, and honey in a big bowl, then transfer them to a baking sheet lined with parchment paper.

Spread out in a single even layer, and roast for about 25-30 minutes, or until the carrots are fork-tender and lightly browned.

The Honey Butter Roasted Carrots recipe is shown here:

https://rasamalaysia.com/honey-butter-roasted-carrots/