BRENTON POINT
WEALTH ADVISORS

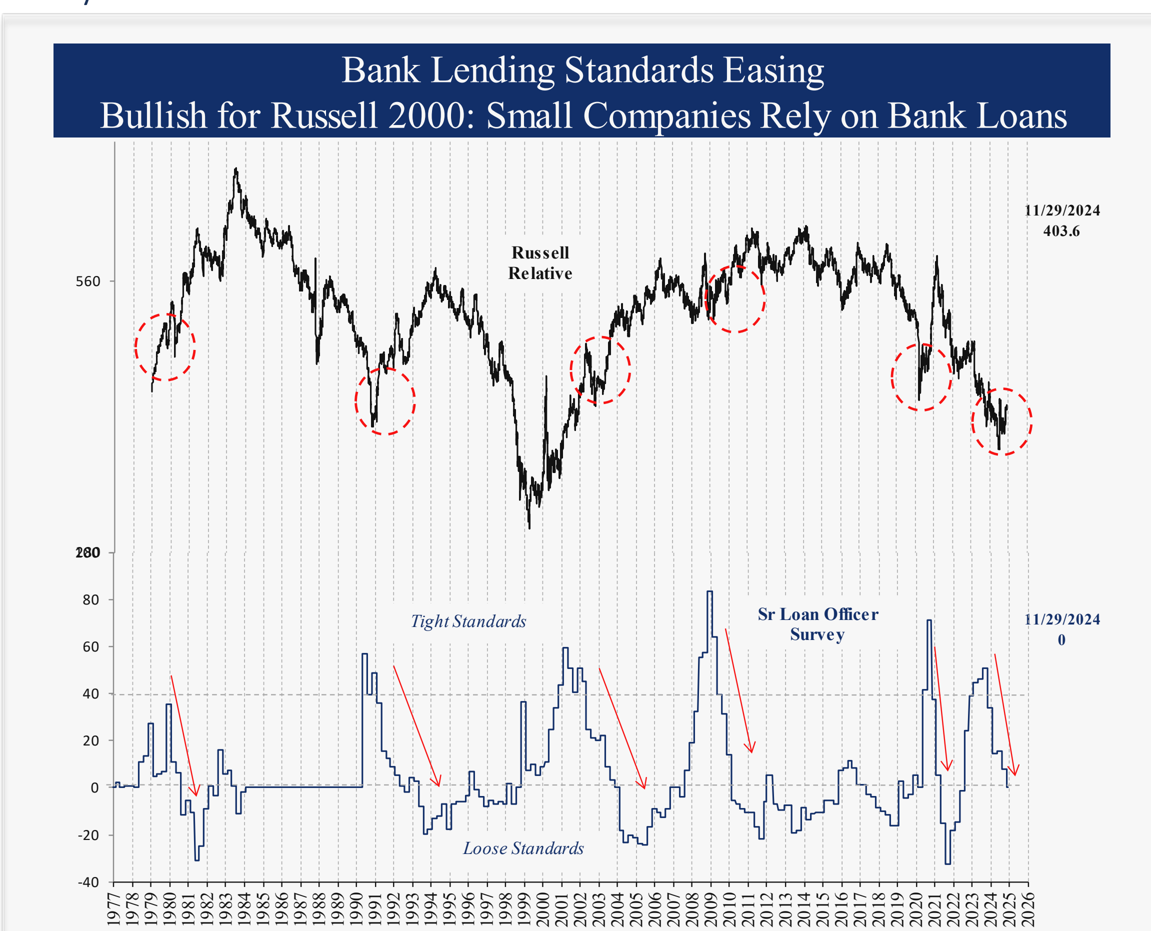
December 3, 2024

Investing Environment Review and Outlook – Volume 87

Last month we discussed the strong performance of gold, the strong Q4 seasonal performance of the S&P, and consumer confidence as a stock market indicator. This month we discuss the strong economic outlook model, the implications of a high real T-bill yield for gold, and the easier bank lending standards effect on the Russell 2000 performance.

Bank Lending Standards Easing Further: Bullish for Russell 2000

The October Fed Senior Lending Officer survey showed easier lending standards from banks than we discussed in August. Small cap companies in the Russell 2000 rely on bank lending for financing, much more than the big cap names that dominate the S&P 500. With easier financing, these companies will find it easier to expand and invest in their businesses. In prior cases lending standards eased, the Russell 2000 reversed persistent underperformance and outperformed the S&P 500, often for the subsequent 2-3 years. With so much focus and media attention on the big cap technology stocks, most investors are ignoring the upside potential of small cap companies trading at lower multiples. Since the relative low on 7/9, the Russell 2000 is up 20.0% vs. just 8.2% for the S&P 500. The long-awaited inflection point for small cap stocks may be in the rear-view mirror.



This review and outlook report by Brenton Point Wealth Advisors LLC represents our views and beliefs regarding the current market outlook. Please also read the important disclosures at the end of this report.

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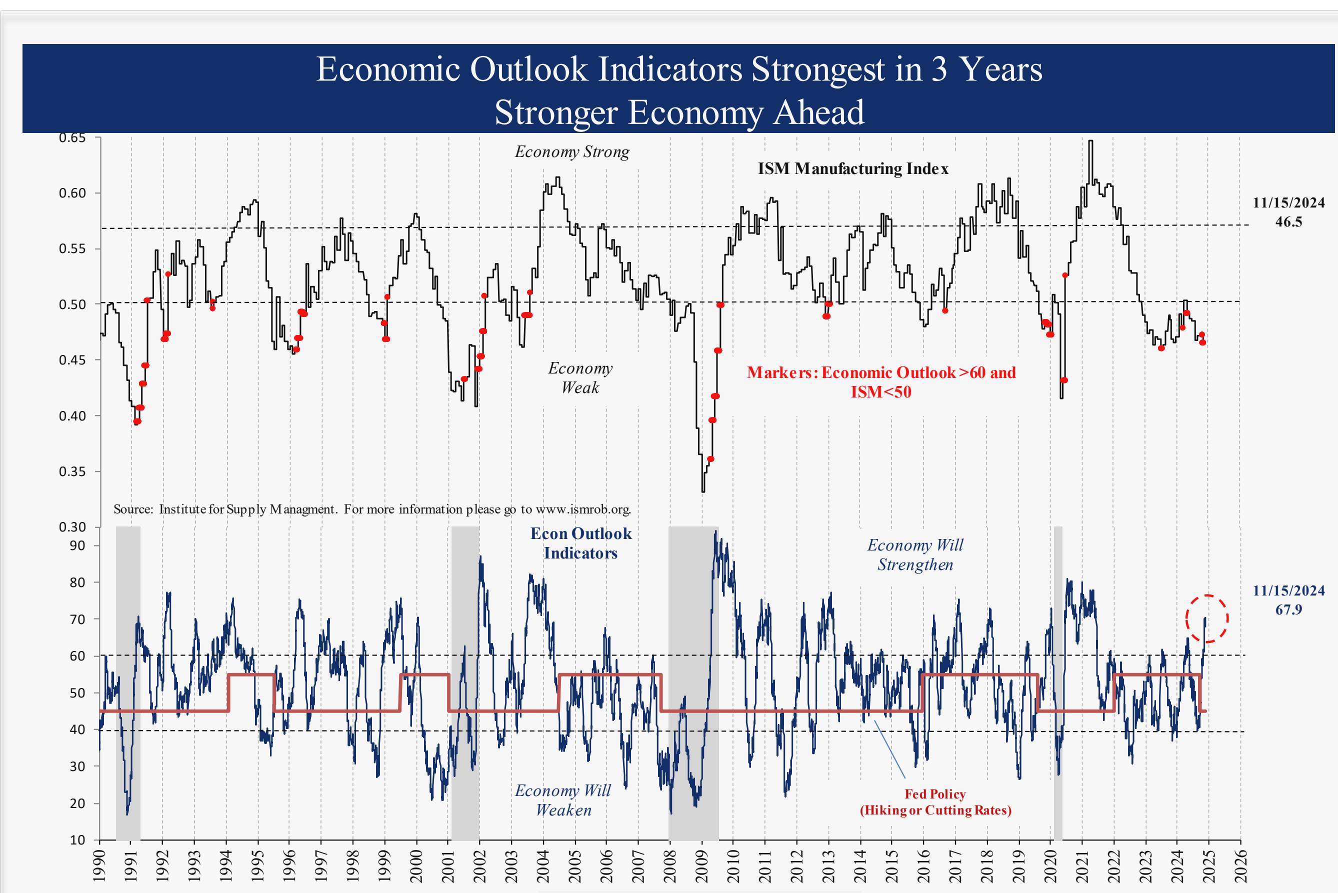
Economic Outlook Model Strong: Bullish S&P 500

Our economic outlook model improved significantly this month to 68, the highest in 3 years. Readings over 60 were followed by a stronger economy and higher ISM Index historically, while readings below 40 were generally followed by a weaker economy. Today's reading of 68 gives us conviction that the economy will be stronger over the next 3-6 months. While we cannot invest in the economy directly, the implications are significant for certain assets. For instance, a strong economic outlook is particularly bullish for the S&P 500 when combined with other conditions like inflation below 4% and a weak manufacturing economy. It means there is slack available in the economy. Other risks remain, such as extreme valuation and investor positioning on the long side.

One interesting point - a strong economic outlook when the economy is strong and inflation is rising translates into negative returns for the S&P 500 historically. This is a great example of the importance of context in the analysis of conditions.



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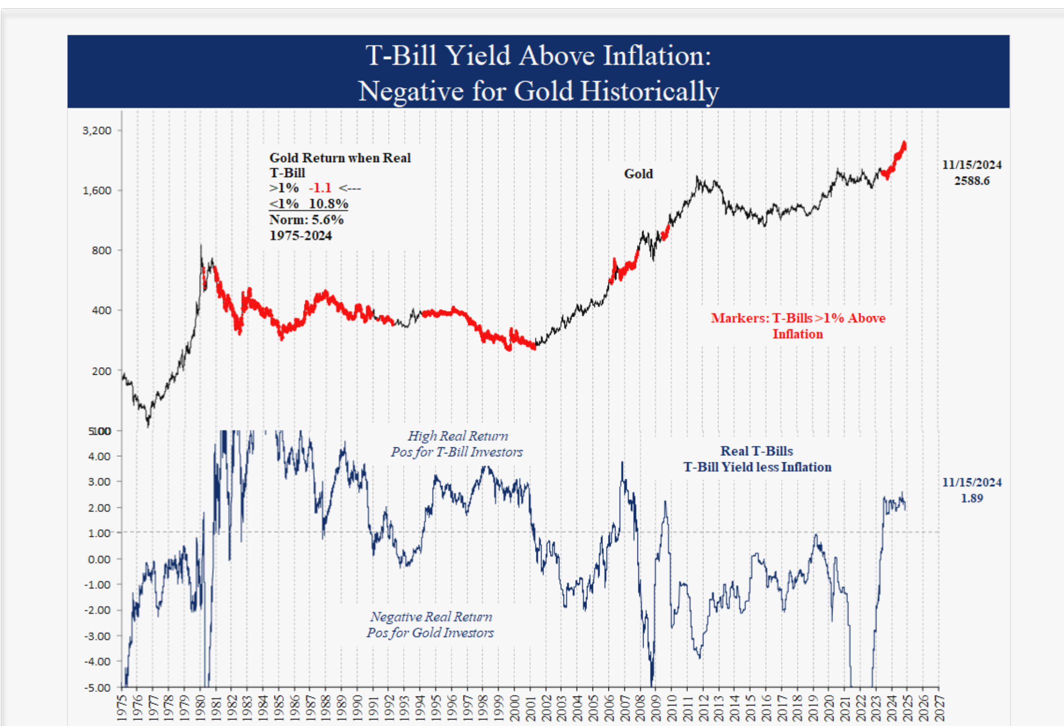
Real T-Bill Yield 1.9%: Negative for Gold

Gold is up 65% from the Oct 2022 low. At that time inflation was 8% and T-Bills were just 4%, for a negative 4% real yield after inflation. In other words, it was a terrible time to hold cash, pushing investors into other assets like equities and gold. Today conditions are much better for cash investors, with the T-Bill yield at 4.5% and inflation at 2.6%, delivering 1.9% real yield to investors. Since 1975, gold returned -1.1% when the real T-Bill yield was greater than 1% as it is today, vs. a 10.8% return when the real yield was less than 1% or negative as it was 2 years ago.

Real yields were negative (and positive for gold) during the biggest gold rally from 1975 to 1980. At that time the Fed was raising short term interest rates, but inflation was higher and rising faster than the Fed hiked. Once Volcker raised rates decisively above inflation to 15% in October 1979, the gold bull market end was near. T-Bill yields were mostly higher than inflation from the 1980 peak to 2001. In other words, cash was attractive to investors, and partly as a result, gold was rangebound to lower for 20 years until 2001. This is a warning sign for gold investors.



We continue to monitor economic and market conditions and analyze their impact on asset classes. Thank you for your support and please contact us with any questions.

Michael Schaus
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