The First Cut

It's always been hazardous to be president of the United States, or even being a candidate campaigning to be president. Seems like there is always someone somewhere who wants to bring you harm, no matter your party affiliation. The 1968 assassination of Robert F. Kennedy (just five years after his brother was assassinated) brought that truth home in the most striking and dramatic manner.

On Friday the 13th this month, someone attempted to assassinate former President Donald Trump for the second time in two months (the previous attempt occurring in July in Butler, Pennsylvania, also on the 13th). Both Democrats and Republicans are accusing the other of "stirring the pot," and inciting violence with their rhetoric. This is not new. And as the election campaign heats up, investors on both sides are wondering (as usual) what happens to our economy (and my investments) if "the other horrible person" wins the election?

This gives us the opportunity to tell you once again that when it comes to your investments, the president of the United States gets way too much credit when the things go well and way too much blame when the things go badly.

Although we don't mean to minimize the importance of the person who is elected to be the leader of the most powerful and successful country in the history of the planet, we want to remind you that there are so many other factors that determine our fate that have very little to do with the Oval Office.

In our July Investment Commentary, we wrote: *In other words, "Sell everything because my guy didn't win" is not necessarily a good investment strategy.*

At BCWM, we will always keep our wits about us.

Seventeen years ago this month, BCWM opened its doors and, at that time, the "Fed Funds Rate" (and the average money-market rate) was about where it is today, a little over 5%. Two weeks later, the Federal Reserve was forced to cut interest rates in response to the unfolding Great Financial Crisis . . . and it didn't stop cutting until it hit 0% at the end of 2008.

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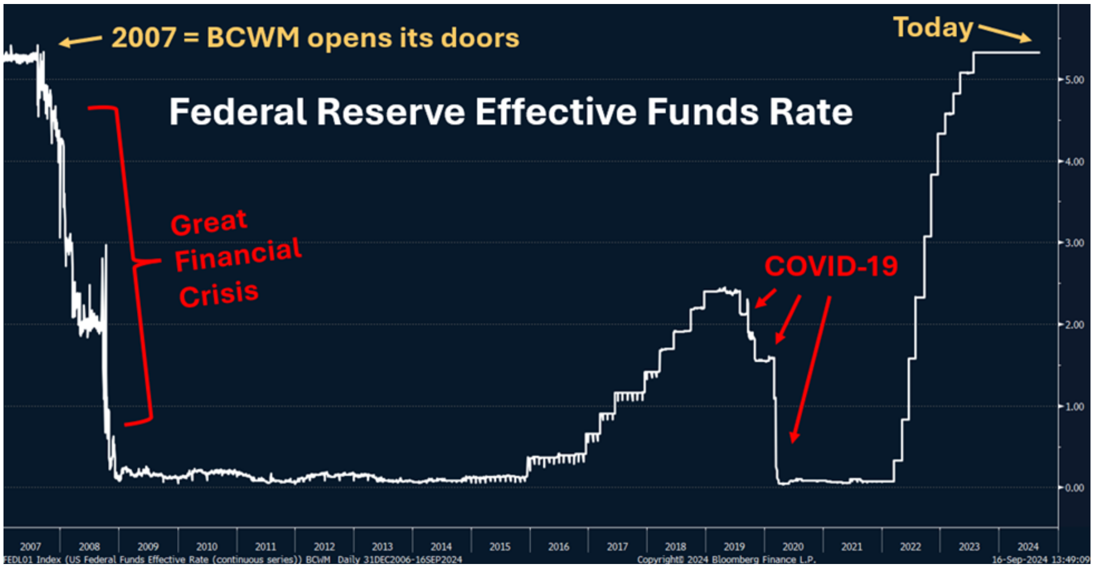


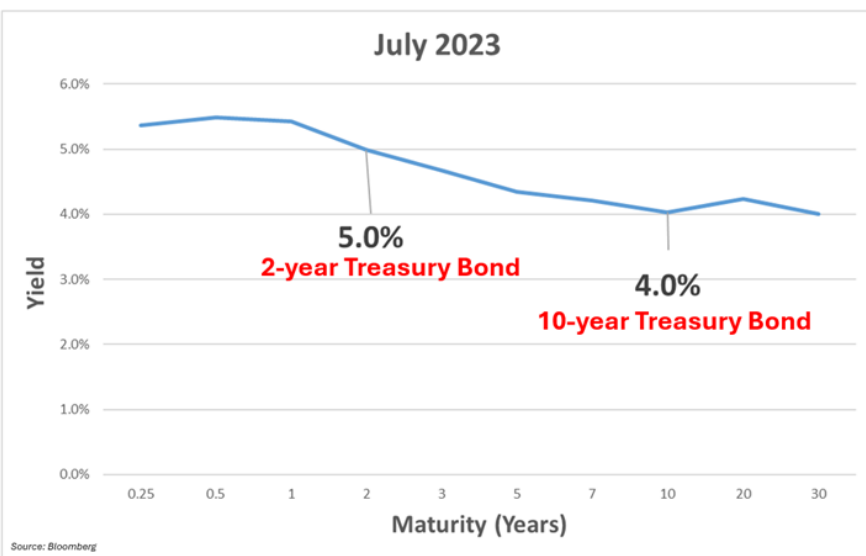
It would take seven years for the Fed to once again *raise* rates, and during those seven years, low interest rates encouraged consumers and businesses to borrow more than they likely would have otherwise. Not a bad idea for getting the economy going, but it didn't come without unintended consequences.

In 2015, the Fed started us on the path to a more normal interest-rate environment by slowly raising rates. COVID put an end to that in 2020. The Fed immediately reduced rates to stimulate an economy ravaged by the COVID shutdowns.

But the inflation caused by the shutdowns and the massive stimulus efforts forced it to raise interest rates again at the fastest pace in decades. Higher interest rates decreased risk-taking behavior (from businesses, entrepreneurs, etc.) and slowed down the economy . . . which was the goal.

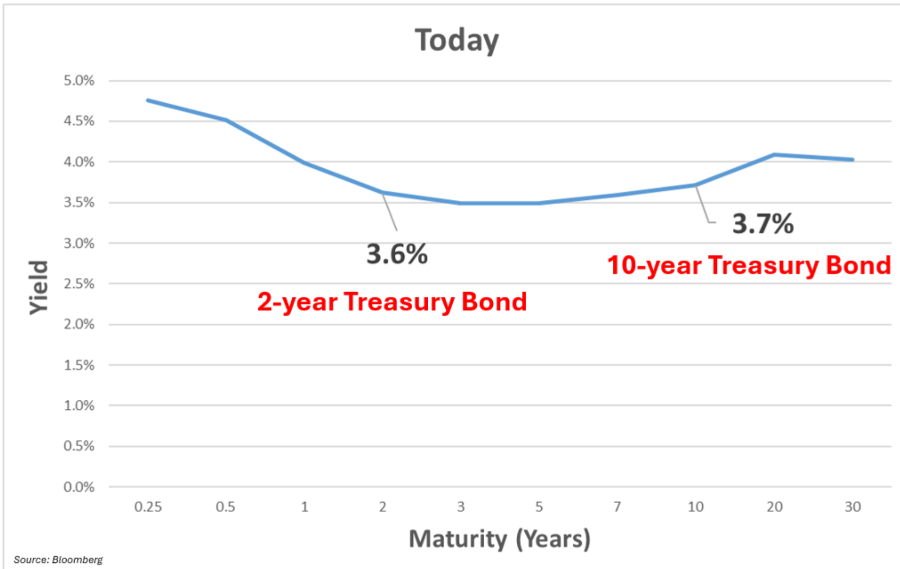
Higher short-term interest rates also made long-term bonds look unattractive. For a few years now, the amount of interest you received for investing in a Treasury bond with a maturity of 10 years was *less* than the amount of interest you could get by investing in a 2-year Treasury bond. By a large amount.

Last summer, many investors were saying, "Why would I invest in a 10-year bond paying me only 4% when I can get a 2-year bond paying me 5%?"



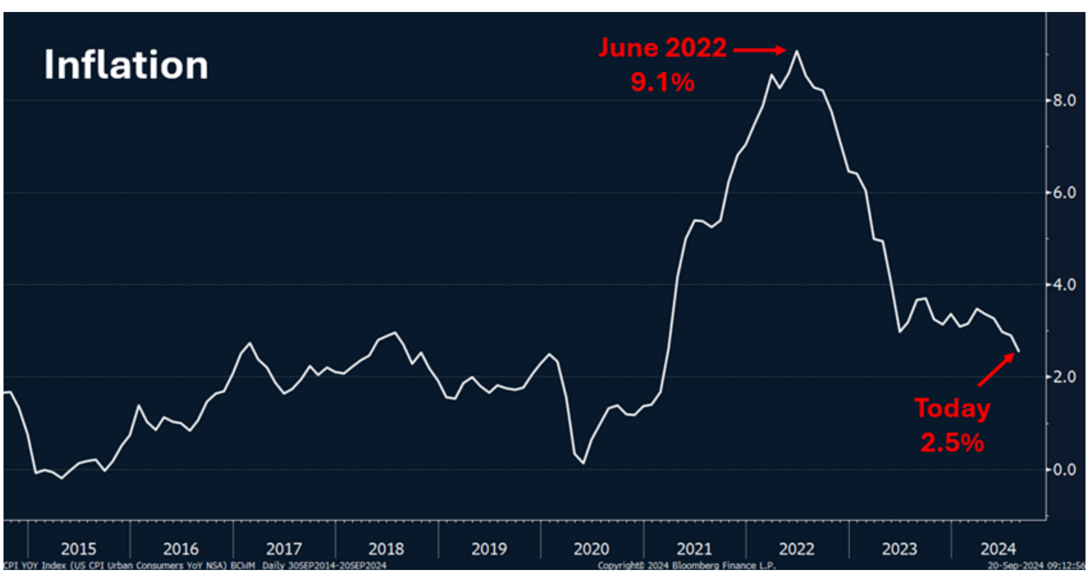
At BCWM, we argued that you should do so because lower interest rates on long-term bonds are a signal that the Federal Reserve is likely to cut short-term interest rates in the future . . . and it's better to own a bond paying you 4% for 10 years than a bond paying you 5% for only two years.

And we were right. A week ago, the Federal Reserve cut short-term rates by 0.50%. This was the first interest rate cut in four years. And here is what those same bonds pay you today:



The expectation is that the Fed will take short-term rates down below 3% by next summer. And those with cash in money-market funds are going to wish they'd bought 10-year bonds today.

Although you don't hear about it in the news, inflation is still a big focus for the Fed. The rapid rate hikes we pointed out in the first graph were a major reason inflation came. But it wasn't until recently that the Fed was able to wrangle inflation closer to its ideal range. Inflation is now running at 2.5%, the lowest rate in three and a half years.



And looking forward, the bond markets are telling us that inflation is going to average about 2% for the next several decades. There are plenty of economists with similar forecasts. These predictions will inevitably be wrong in any given year, but the takeaway here is that, barring a major unforeseen shock (like a pandemic, war, or supply-chain disruption), inflation should remain low for the foreseeable future.

We will discuss the future path for inflation, along with our thoughts on the market, the election, the U.S. dollar and more in our upcoming webinar scheduled for Thursday, October 24, at 1 p.m. CDT. Be on the lookout for an email with registration details.

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