November 2023

From the front page of Friday's WSJ:

Stocks Log Their Strongest Month Since ’22

Dow hits yearly high, bonds end November strong as inflation data cheer investors

BY RYAN DEZEMBER

U.S. stocks recorded their best month in more than a year, with the Dow Jones Industrial Average climbing Thursday to a 2023 high, while bonds posted their biggest monthly gain in years.

Commerce Department data on Thursday showed that U.S. consumers slowed their spending and that inflation continued to ease in October, boosting expectations that the Federal Reserve is done raising rates.

All three major U.S. stock indexes ended November at least 8% higher, snapping three-month losing streaks. The tech-heavy Nasdaq Composite led the way, ending the month up 10.7% .... The S&P 500 ... finished November 8.9% higher.

The blue-chip Dow ... had its best month since October 2022, climbing 8.8% to its highest close since January 2022.

November’s gains were accompanied by a bond rally that drove the yield on the 10-year U.S. Treasury note down to 4.349% on Thursday, from just above 5% in late October. The benchmark yield recorded its biggest monthly slide since 2019. ...

The stocks that led the equities rally were generally in sectors most sensitive to borrowing costs, including information technology, real estate and finance, along with companies that rely on consumer discretionary spending. Those segments of the S& P 500 climbed at least 10% during the month.

Real-estate stocks had their biggest monthly increase since October 2011, when they were climbing back from the depths of the foreclosure crisis.

The rally in stocks began after yields peaked in October, picking up steam midmonth after data showed consumer prices fell by more than Wall Street expected. Thursday’s data showed that the personal-consumption expenditures price index, the Fed’s preferred inflation gauge, remained mild in October. ,,,

John Williams, president of the Federal Reserve Bank of New York, said in a speech Thursday that, while he sees inflation eventually declining toward the central bank’s 2% target, he isn’t ready to loosen the Fed’s grip on the economy quite yet.

“Inflation is still too high,” Williams said. “I expect it will be appropriate to maintain a restrictive stance for quite some time to fully restore balance and to bring inflation back to our 2% longer-run goal on a sustained basis.” ...

Oil prices declined despite the Organization of the Petroleum Exporting Countries and their market allies agreeing to further reduce output to support prices. Benchmark U.S. oil futures shed $1.90 a barrel to close Thursday at $75.96, down 6.2% on the month.

Major overseas indexes mostly rose in November. The Stoxx Europe 600 added 6.4% for the month. Japan's Nikkei 225 index, ... saw a monthly gain of 8.5% .... Hong Kong's Hang Seng ended November 0.4% lower ....

Two from Bespoke. On Friday:

A Flat 2 Years

This morning we wanted to share with you our asset class performance matrix that highlights recent total returns for various ETFs and other exchange traded products. It was an extremely strong month for US equities across the board, while many country ETFs did even better than the US. Also noteworthy is that as well as the S&P 500 (SPY) did in November with a gain of 9.1%, the 20+ Year Treasury ETF (TLT) did even better at +9.9%!

On a separate note, it's remarkable that with all the talk of how well the mega-caps are doing versus the rest of the market, just five basis points separates the mega-cap Nasdaq 100 (QQQ) and the S&P 500 Equalweight (RSP) on a two-year total return basis. QQQ is up a whopping 2 basis points over the last two years while RSP is down 3 basis points. That's right, both QQQ and RSP are basically flat over the last two years.

And get this... S&P 500 close on 11/30/23: 4,567.80 ... on 11/30/21: 4,567.00

Asset Class Performance November, YTD, and Last 2 Yrs - Total Return (%)

US Related

ETF	Description	November	YTD	Last 2 Yrs
SPY	S&P 500	9.13	20.68	3.32
DIA	Dow 30	9.15	10.58	8.52
QQQ	Nasdaq 100	10.82	46.66	0.02
IJH	S&P Midcap 400	8.50	7.09	-2.18
IJR	S&P Smallcap 600	8.27	2.92	-9.86
IWB	Russell 1000	9.33	20.39	1.14
IWM	Russell 2000	9.20	4.20	-15.26
IWV	Russell 3000	9.34	19.48	0.07
IVW	S&P 500 Growth	8.70	25.13	-9.60
IJK	Midcap 400 Growth	7.59	9.26	-7.99
IJT	Smallcap 600 Growth	7.46	4.41	-13.85
IVE	S&P 500 Value	9.57	15.66	17.10
IJJ	Midcap 400 Value	9.54	4.58	2.93
IJS	Smallcap 600 Value	9.07	1.19	-6.58
DVY	DJ Dividend	7.01	-4.35	4.47
RSP	S&P 500 Equalweight	9.18	6.44	-0.03
FXB	British Pound	4.04	7.12	-2.50
FXE	Euro	3.08	3.21	-3.33
FXY	Yen	2.19	-11.93	-24.65
GBTC	Bitcoin Trust	13.02	264.84	-34.56
ETHE	Ethereum Trust	18.33	244.54	-64.18
XLY	Cons Disc	10.97	31.57	-16.03
XLP	Cons Stap	4.13	-3.44	5.77
XLE	Energy	-0.72	-0.71	67.89
XLF	Financials	10.94	6.44	-1.64
XLV	Health Care	5.44	-2.17	4.43
XLI	Industrials	8.83	10.33	9.80
XLB	Materials	8.35	7.59	1.51
XLK	Technology	12.90	49.75	11.74
XLC	Comm Services	7.80	46.38	-5.71
XLU	Utilities	5.14	-8.87	1.38

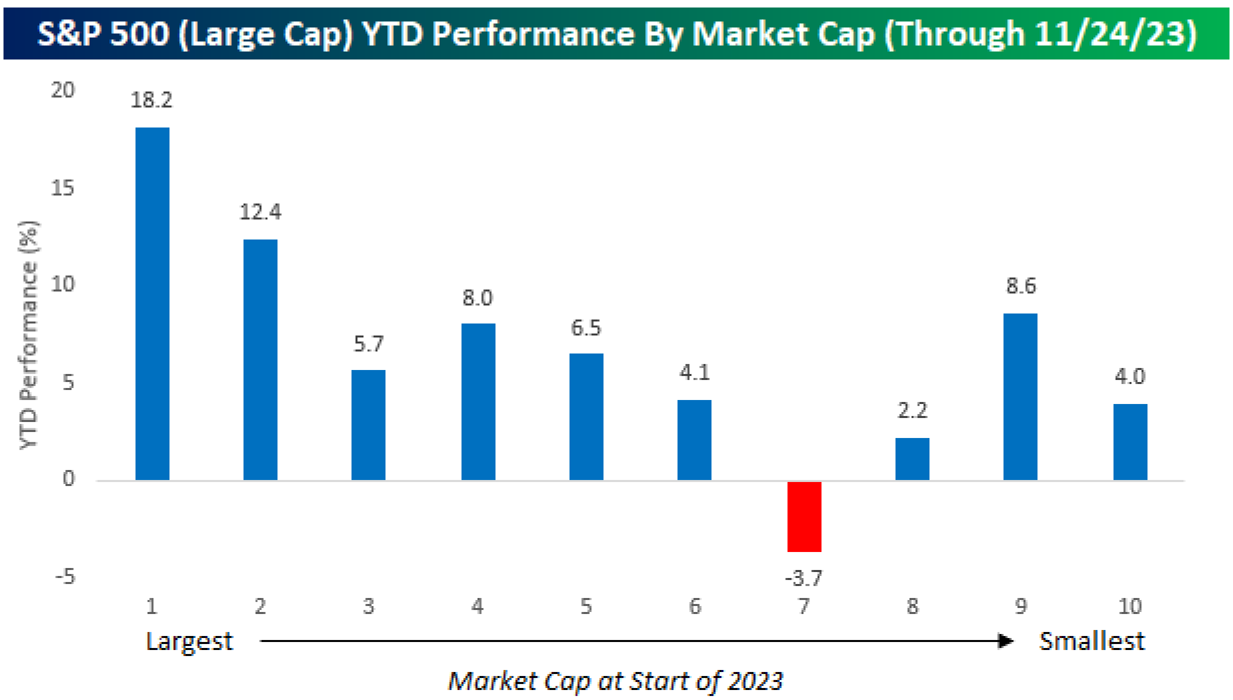
Global

ETF	Description	November	YTD	Last 2 Yrs
EWA	Australia	8.24	2.90	1.92
EWZ	Brazil	14.24	24.58	45.83
EWC	Canada	10.21	7.96	-2.13
ASHR	China	-0.28	-11.38	-34.18
EWQ	France	9.06	15.97	7.92
EWG	Germany	12.83	18.04	-4.55
EWH	Hong Kong	0.18	-18.70	-23.72
PIN	India	6.78	15.11	7.21
EWI	Italy	10.30	25.42	13.97
EWJ	Japan	6.19	15.82	-2.52
EWW	Mexico	15.40	28.83	47.75
EWP	Spain	14.05	27.84	27.70
EIS	Israel	16.28	-2.19	-25.39
EWU	UK	6.20	7.69	9.45
EFA	EAFE	8.22	12.37	0.49
EEM	Emerging Mkts	7.79	5.20	-15.15
IOO	Global 100	8.44	23.43	7.94
BKF	BRIC	5.03	0.17	-22.62
CWI	All World ex US	8.16	10.29	-2.92
DBC	Commodities	-2.45	-3.00	23.48
DBA	Agric. Commod.	1.23	10.57	15.65
USO	Oil	-6.50	0.04	46.40
UNG	Nat. Gas	-26.40	-60.85	-63.40
GLD	Gold	2.53	11.27	14.05
SLV	Silver	10.25	5.04	9.83
SHY	1-3 Yr Treasuries	1.05	3.03	-1.18
IEF	7-10 Yr Treasuries	4.55	-0.12	-15.71
TLT	20+ Yr Treasuries	9.92	-5.43	-36.29
AGG	Aggregate Bond	4.59	1.89	-11.70
BND	Total Bond Market	4.54	2.03	-11.63
TIP	T.I.P.S.	2.77	1.34	-10.71

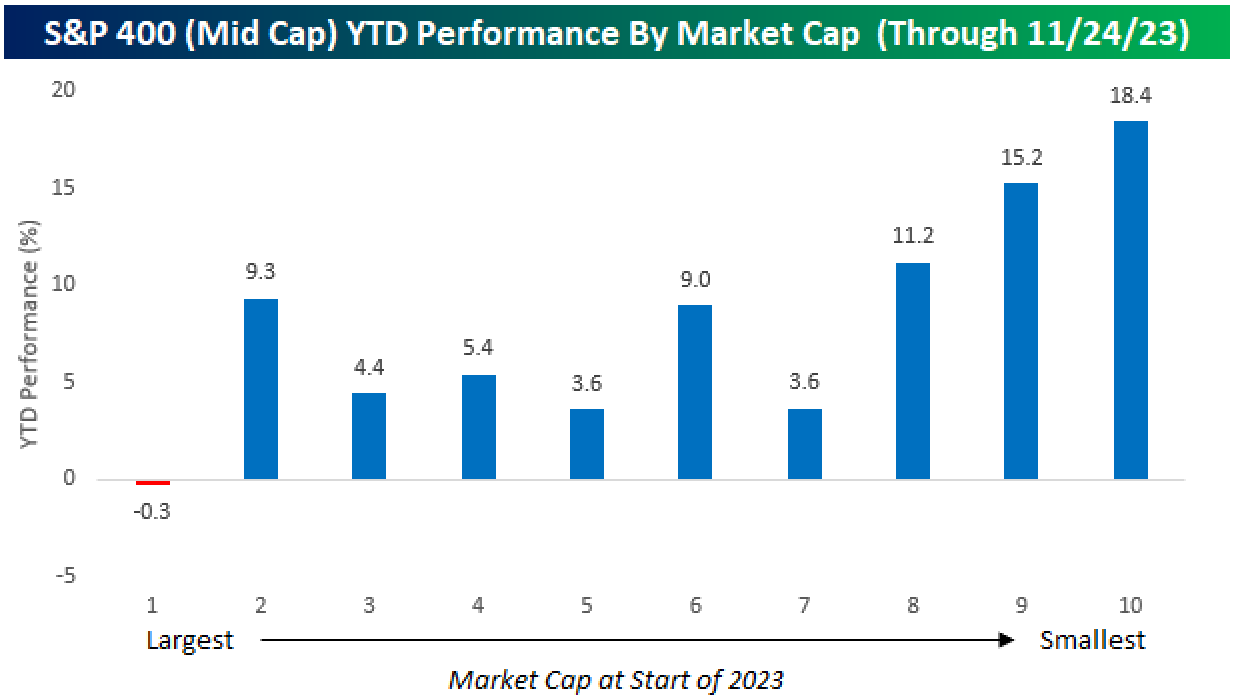
Not Necessarily the Mega Caps and Everyone Else

Mon, Nov 27, 2023

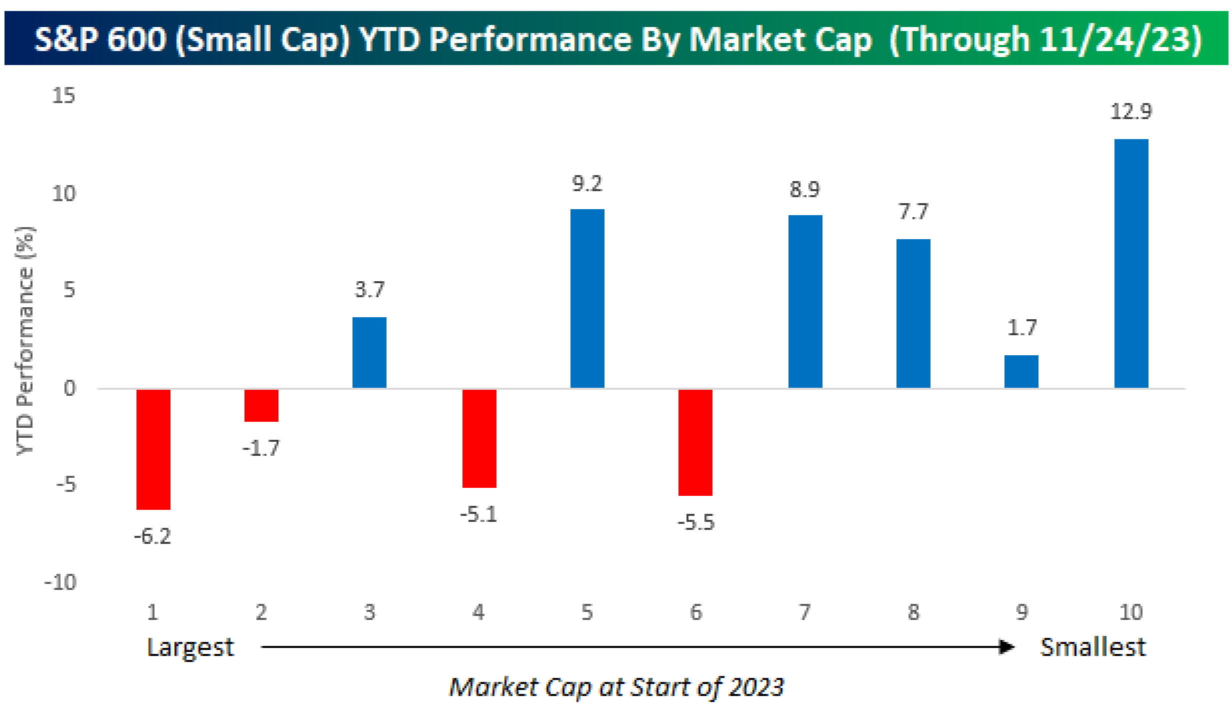
You would have to be living under a rock this year to not know that the performance of US stocks has been driven in large part by companies with the highest market caps. To illustrate it again, the chart below summarizes the YTD performance of stocks in the S&P 500 based on where their market caps stood at the beginning of the year. The first decile on the left in the chart contains the 50 stocks in the S&P with the largest market caps at the start of 2023, and so on and so forth until you get to the last decile which contains the 50 stocks in the index with the smallest market caps at the start of the year. As shown, the 50 stocks with the largest market caps at the beginning of the year are up an average of 18.2% YTD, and a lot more than any other of the nine deciles. In the S&P 500, this year has been all about the largest stocks and everybody else.



With the largest stocks in the S&P 500 trouncing the rest of the index, we were curious to see if there was a similar dynamic at play among mid-cap stocks (S&P 400) and small-caps (S&P 600), and we were surprised to see the opposite trend at play. Starting with stocks in the S&P 400 Mid Cap index, the 40 largest stocks in that index are down an average of 0.3% YTD, and every other decile of stocks in that index is up YTD. In fact, the three deciles comprising the stocks with the smallest market caps at the start of the year are all up by double-digit percentages YTD. Some reports would have you believe that the mega-caps are the only area of the market that has rallied this year, but stocks in the decile of the smallest stocks in the S&P 400 are actually up more, on average, than the stocks that make up the 50 largest stocks in the S&P 500.



Within the small-cap space, stock performance by market cap has been somewhat less correlated, although we would note that four of the six deciles with the largest stocks by market cap at the start of the year are down YTD. Meanwhile, deciles seven through ten, which are comprised of the 240 stocks in the index with the smallest market caps, are all up YTD.

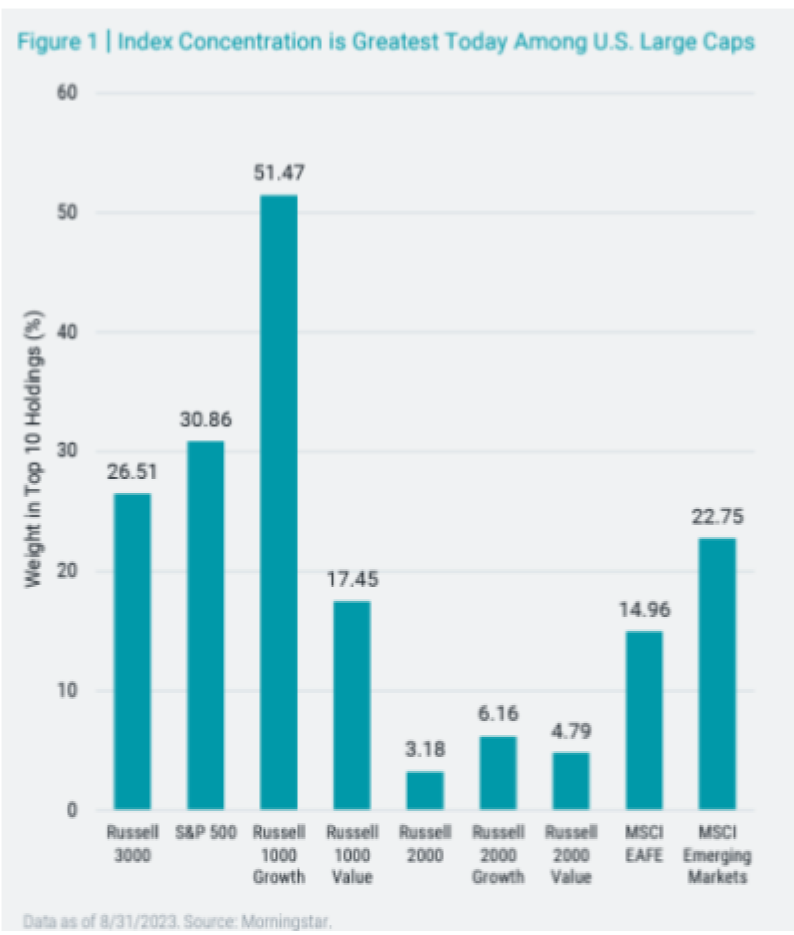


The Magnificent Seven

By Larry Swedroe | November 17th, 2023

As the head of financial and economic research at Buckingham Wealth Partners, I've been getting lots of questions about The Magnificent Seven—not the movie, one of the greatest westerns of all time starring Yul Brynner and Steve McQueen, but Apple (+35.2%), Amazon (+50.0%), Microsoft (+34.1%), Nvidia (+205.9%), Alphabet (+53.3%), Tesla (+111.1%), and Meta Platforms (+153.3%). Through October 5, 2023, these stocks had returned an average of almost 92%. Together they account for basically the entire 12.4% gain of the S&P 500 Index—an equal-weighted version of the S&P 500 would have returned just 0.1%. What, if any, implications does such a dramatic dispersion in returns have for investors?

While the performance of these stocks has been spectacular, it has led to the increased concentration of market-like portfolios, reducing the benefits of diversification and increasing a portfolio's exposure to idiosyncratic risks. While market-cap-weighted indexes, by their nature, will have some concentration of risk in the largest stocks, thanks to the research team at Avantis, we can see that concentration levels for the 10 largest stocks in several common indices are now at historical highs. As Figure 1 below shows, while the concentration level for the S&P 500 Index was almost 31% at the end of August, it exceeded 51% for the Russell 1000 Large Growth Index. In contrast, the concentration level for the Russell 1000 Large Value Index was about 17% and about 15% for the MSCI EAFE Index. Concentration risk is dramatically lower in the small-cap indices: about 3% for the Russell 2000, about 6% for the Russell 2000 Growth, and less than 5% for the Russell 2000 Value.



The following chart shows that concentration levels have increased dramatically in recent years, while the levels for the smaller cap and value indices have been relatively stable. Note also that they are now significantly higher for the Russell 1000 Growth and S&P 500 Indices than before the dot-com bubble bursting in March of

2000. On the other hand, the concentration levels for the Russell 2000 and the Russell 1000 Value indices are at or near their lowest levels.

Figure 2 | U.S. Large Cap and Large Growth Index Concentration Has Been on the Rise

The next table shows the historical concentration levels for various indices, including their minimum, maximum, and average concentration levels.

Figure 3 | Indexes Holding U.S. Large Growth Stocks Are Currently at Concentration Level Highs While Other Indexes Are Near or Below Avg.

INDEX	AUGUST 2023	PERIOD MAX	PERIOD MIN	PERIOD AVG.
Russell 3000	26.51	26.51	13.65	17.97
S&P 500	30.86	30.86	17.01	21.67
Russell 1000 Growth	51.47	51.47	17.14	30.19
Russell 1000 Value	17.45	34.51	16.22	24.37
Russell 2000	3.18	8.55	1.63	2.86
Russell 2000 Growth	6.16	12.07	3.07	5.23
Russell 2000 Value	4.79	9.16	2.93	4.47
MSCI EAFE	14.96	17.28	10.87	13.22
MSCI Emerging Markets	22.75	32.45	15.10	20.51

Data from 1/31/2000 – 8/31/2023. Source: Morningstar.

What, if any, are the takeaways for investors?

Investor Takeaways

The data shown shouldn’t cause you to believe that the market is a bad investment simply because a subset of large companies constitutes a large portion of the overall market. However, when a small subset of companies makes up a large portion of a portfolio, for better or worse their returns will have a greater impact on overall portfolio results. Thus, the increased concentration of market cap and growth indices has led to increased portfolio risk. Investors should also be concerned that the increased concentration has been created by the dramatic rise in the valuations of the Magnificent Seven, which increased by far more than their earnings. The historical evidence clarifies that higher valuations typically lead to lower future returns.

Consider that as of October 6, 2023, while the iShares Russell 1000 Growth ETF (IWF) had a P/E of 24.2 and Vanguard's S&P 500 ETF (VOO) had a P/E of 20, the P/E of the Vanguard Russell 1000 Value ETF (VONV) was 15, the P/E of the Vanguard Russell 2000 ETF (VTWO) was 13.3, and the P/E of the Vanguard Russell 2000 Value ETF (VTWV) was just 10.5. Now consider the P/Es of the magnificent seven: Apple, 29.8; Amazon, 100.7; Microsoft, 33.8; Nvidia, 110.5; Alphabet, 29.4; Tesla, 73.8; and Meta Platforms, 36.8. That's an average P/E of 59.3.

History's Lessons

... let's review the list of the 10 largest stocks by market cap in the S&P 500 Index at the turn of the century. They were Microsoft, Cisco Systems, Exxon Mobil, Intel, Citigroup, IBM, General Electric, Oracle, and Home Depot. From January 2000 through September 2023, Vanguard's 500 Index Fund (VFINX) returned 6.5% per annum. How did the top 10 perform?

- Microsoft: 9.5%
- Cisco Systems: 1.6%
- Exxon Mobil: 7.9%
- Intel:1.7%
- Citigroup: -7.1%
- IBM: 3.8%
- General Electric: -1.8%
- Oracle: 6.6%
- Home Depot: 8.6%
- AT&T: 1.4%

The average return to the 10 largest stocks in the S&P 500 Index from January 2000 through September 2023 was just 3.2%, underperforming the index itself by 3.3 percentage points. Because these were the largest stocks, the underperformance relative to the remaining 490 stocks was even worse. Investors in the top 10 stocks took a much greater degree of idiosyncratic risk and earned lower returns. Forewarned is forearmed.

Done properly, diversification of risk is an investor's friend, reducing the volatility of a portfolio without reducing its risk-adjusted expected returns. On the other hand, concentrated portfolios increase the potential dispersion of outcomes without increasing expected returns. Thus, all else equal, less-concentrated portfolios should be preferred. One way for investors to diversify the risk of concentration, as well as high valuations, is to move their allocations more toward value strategies, which over the long term have produced above-market returns.

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Positions

DAR - On 10/19 JP Morgan lowered their Target Price (TP) from 91 to 76, while maintaining their Overweight Recommendation. This caused DAR to drop 5.4% on 2.2 times normal volume on the 20th. On 11/7 DAR released 3Q earnings with a 2.4% Positive Surprise. However, several analysts significantly lowered their Earnings Estimates for the next 2 quarters, and 7 analysts lowered their TP, while 5 maintained theirs. On 11/15 we sold for 4 clients at 44.41.