May 2022

Gore Capital Management

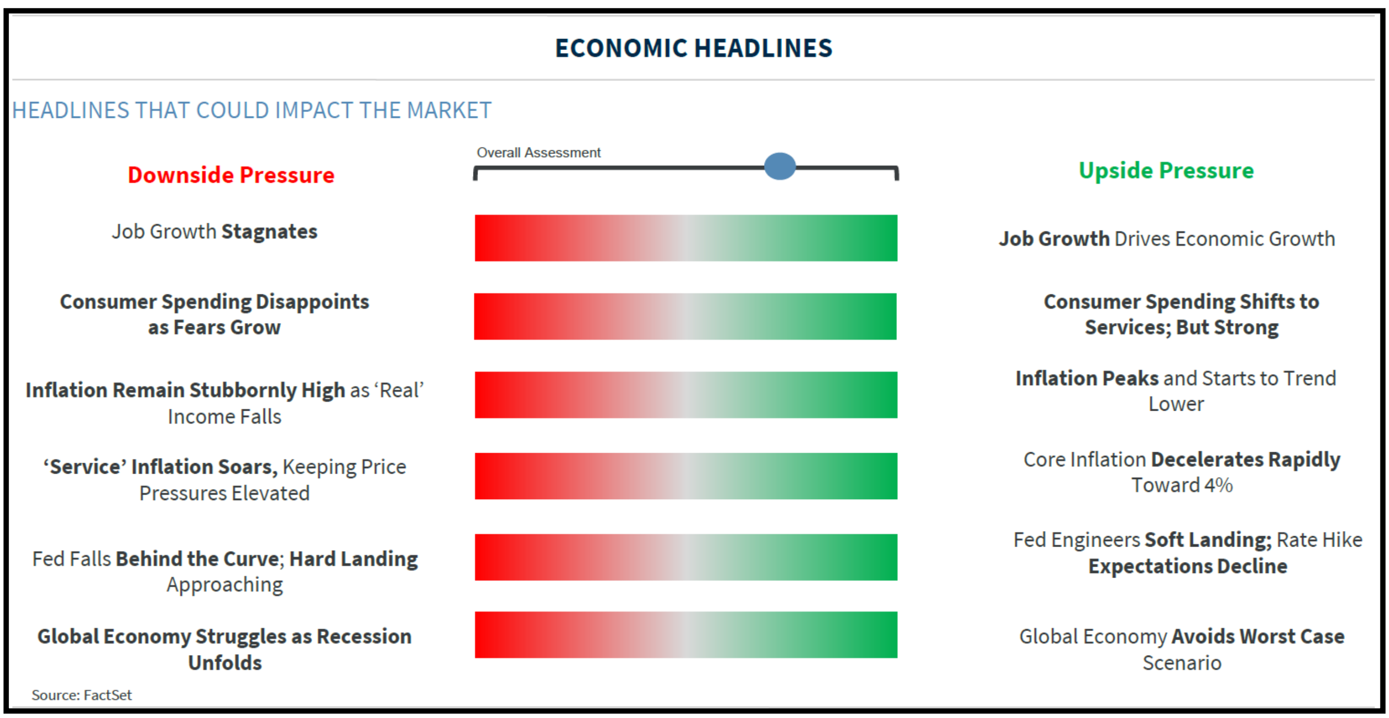
Our only client is you.

“The stock market is a device for transferring money from the impatient to the patient”

- Warren Buffet

With everything that’s happened over the past 3 months, it feels like ages since we released a newsletter. At the time of our last publication, nobody was at war, the S&P 500 index was down ~5% from all-time highs, and inflationary pressures were expected to subside in the spring. Given the state of things now, the AAII bullish sentiment survey is near its lowest level in almost 20 years (RJ “Should You Stay or Should You Go” webinar, 5/12/22). In our ongoing effort to combat emotion with objective fact, we will try to keep our newsletter focused on the data.

First quarter 2022 earnings season is nearly concluded with all but about 10% of the S&P 500 reporting earnings as of this writing. Results have generally been very strong, with average earnings growth for the S&P 500’s constituents estimated to be over 9% for the quarter ending 3/31. This figure is about 4% higher than analysts’ estimates, implying that corporate America is actually in better shape than analysts were expecting. One item of note: many of our readers likely saw Amazon’s earnings “miss” reported a few weeks ago. While the company did in fact fail to meet analysts’ expectations for earnings, it’s important to acknowledge that Amazon still generated $116.4 billion in revenues and only reported negative earnings because of a paper loss in their stake of electric truck maker Rivian (Data from Amazon’s 1Q report and Factset, 5/6/22). This was the case with a number of other high profile earnings misses as well; companies still reported strong results despite not quite meeting analysts’ lofty expectations.



Market Statistics	April ‘22	YTD	2021	3-Year Annl.	5-Year Annl.
S&P 500	-8.74%	-13.03%	28.16%	13.27%	13.05%
Dow Jones Ind. Avg.	-4.85%	-8.88%	20.28%	9.06%	11.22%
Russell 2000 (Small Cap)	-9.92%	-16.77%	14.49%	6.35%	6.85%
MSCI EAFE (Foreign)	-6.47%	-12.00%	11.26%	4.44%	4.77%
MSCI ACWI (Global)	-8.00%	-12.94%	18.54%	9.41%	9.46%
MSCI Emerg. Mkts. Equity	-5.56%	-12.15%	-2.54%	2.24%	4.32%
Barclay’s Aggregate Bond	-3.79%	-9.50%	-1.54%	0.38%	1.20%
iShares Gold ETF (GLD)	-2.16%	4.54%	-3.51%	14.14%	8.55%

Source: Morningstar, as of 4/30/22

Thanks to the combination of good earnings growth and terrible market performance over the past few months, the S&P 500's price-to-earnings ratio is now under 18. This is below the most recent 5-year average ratio of 18.6 (which takes us back to pre-COVID) but a little higher than the 10-year average (post-Great Recession). Our readers will recall that we have mentioned the S&P's elevated P/E ratio in several of our recent newsletters. The P/E ratio is not a forecasting tool for future market returns – the market can and often does behave irrationally for extended periods of time – but it does tell us that stock prices are not unreasonable compared to history. The fact that earnings for the full 2022 calendar year are still expected to reach a record $229 per share for the S&P 500 should give investors confidence that the economy is not on the verge of imminent collapse. (Data from Factset, 5/6/22)

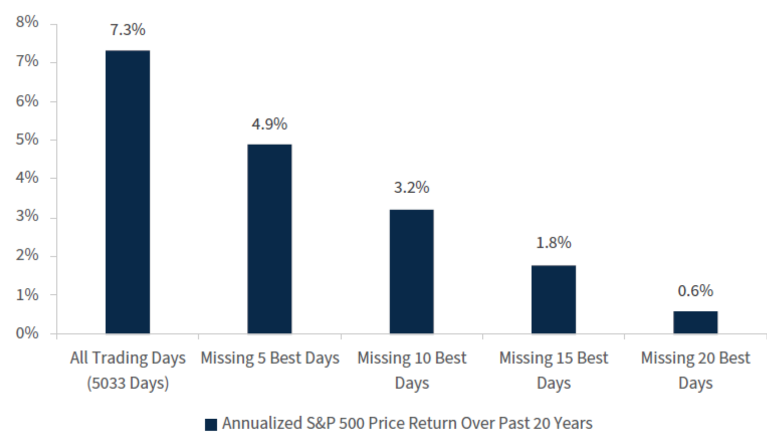
Speaking of the economy, headline GDP for the first quarter declined 1.4% due in large part to growth in our trade deficit (more imports than exports) and a reduction in defense spending. Importantly, consumer spending (roughly 2/3rds of economic activity) remained solid, rising 2.7% (CNBC). One quarter of negative growth does not constitute a recession, and full-year economic output is still expected to rise 3.2% in 2022 (S&P Global). Many analysts believe a recession is not on the imminent horizon, but acknowledge the risk is growing; Goldman Sachs estimates a 35% chance within the next 12 months and Deutsche Bank forecasts a recession could come late next year or early into 2024 (CNBC). In the meantime, economic indicators remain mostly positive. Unemployment is approaching pre-pandemic lows and withholding taxes and consumer cash balances are at record highs (RJ webinar, 5/12/22).

The Federal Reserve remains in a difficult spot, with the economy in reasonably good shape but inflation still red hot. Despite the many calls for pressures to subside as the year progresses, May's CPI reading was 8.3% year-over-year, near the highest level recorded since the early 1980s (CNBC). Until we start to see these readings come down, investors will stay worried that the Fed will have to raise rates at a faster clip than they anticipate in order to get prices under control. Though Jerome Powell and his team try to be as transparent as possible in order to manage investor expectations, the Fed's dual mandate of price stability and full employment does not include "keeping the market happy," and they will ultimately take whatever actions they feel are necessary if inflation does not begin to stabilize in the near future.

Fortunately, there are some signs prices might be stabilizing. Used car prices have fallen more than 6% from the highs reached late last year and WTI crude oil prices have fallen about 10% from the highs in March (oil remains awfully volatile, though). Supply chain pressures, often cited as a primary reason for persistent inflation, are also starting to show signs of easing. Inventories are rising, delivery times are dropping, and trucking freight costs are declining. These are positive indicators, but the data is likely too "young" to draw any meaningful conclusions about trends just yet (RJ webinar, 5/12/22).

Range of best and worst annual returns

Historically, the market has tended to deliver more consistent, positive returns the longer the investment is held. The chart below looks at rolling returns over various holding periods.



As of 12/31/21. Source: Raymond James Investment Strategy research. This example is for illustrative purposes only and is not indicative of the performance of any investment. It does not reflect the impact of taxes, management fees, or sales charges. The S&P is a weighted, unmanaged index composed of 500 stocks believed to be a broad indicator of stock price movements. Investors cannot buy or invest directly in market indexes or averages. Past performance is no guarantee of future results.
Dollar-cost averaging does not assure a profit and does not protect against loss. It involves continuous investment regardless of fluctuating price levels of such securities. Investors should consider their financial ability to continue purchases through periods of low price levels.

The political scene in Washington has taken a back seat as of late. Tax reform and the Build Back Better agenda seems to have been put on hold while our executive and legislative branches grapple with inflation and the war in Ukraine. Rising prices is top of mind for voters right now, and although they don't have a lot of power to calm inflation, Democrats are going to face a very stiff battle come November unless things change meaningfully soon.

The tone of this newsletter is a bit less cheery than usual. While we remain optimistic for the long-term prospects of our country, it's clear that volatility is likely here to stay for the near-term as the market and the American people come to terms with some real challenges. This does not mean we are deviating from our course. Volatility is normal, with the S&P 500 experiencing at least one decline of 10%+ on average every year. When markets become irrational, extreme down days are often followed up with extreme up days. Missing even just a few of these good days can have a dramatic negative effect on long-term returns (see chart nearby). Bear markets (losses of 20%+) are less common, occurring on average every 3-4 years (Hartford). However, when a bear market is not accompanied by recession (our opinion at this point), the market is historically back to even within 10 months on average. Losses never feel good but staying the course has historically proven to be the right strategy.

We know market volatility can be frustrating to say the least. Please don't hesitate to reach out to discuss your financial plan and our thoughts on the market in more detail. We welcome the conversation.

Ben’s Corner

Many of you may know I recently became a new dad. We’re only a few weeks into this experience, but so far so good. In addition to the many joys of parenting and watching Philip grow, I’m also glad he will provide me some inspiration for newsletter editorials. The finances of raising children is an interesting subject which can be explored many different ways. One of the most significant costs many parents, especially brand-new parents, face is the cost of actually *having* the child. Thanks to our confusing health insurance system, we have no idea what my wife’s pregnancy and delivery will cost us out of pocket yet.

Throughout my wife’s pregnancy, we received in the mail a number of “explanation of benefits” (EOB) statements from our health insurance company. Surely my readers are familiar with these cryptic documents which detail how much a medical care provider says a service costs, the amount the health insurance company thinks it should cost and is willing to pay, and the amount you may owe. It seems to me that service providers intentionally inflate the cost of their service knowing full well the insurance company will pay less. It’s like negotiating with someone on Craigslist – you always ask for more than you expect to receive.

Looking at these EOBs and seeing the enormous figures on some of them got me thinking about the healthcare system here in America. We had an excellent experience overall, but it sure was costly to our insurance company. Not to mention, as I said before, we still don’t know what the whole thing will cost us out of pocket. There is no way I can offer a complete, in-depth analysis of health care in America in one short page, so I’ll focus on a few interesting statistics I turned up in my research. Before I begin, I want to make very clear that this is not a crusade against doctors or health care professionals. This is an objective reporting of data collected by what I believe to be high-quality and (mostly) non-partisan sources including the Kaiser Family Foundation, *Health Affairs*, and the Congressional Budget Office.

The United States spends more on health care per capita than every other wealthy nation, roughly double the amount spent by the average nation in our peer group (Switzerland, Canada, Germany, Sweden, etc.). More spending means better outcomes, right? Surprisingly, no:

- Average life expectancy in the US is about 5 years lower than our peer group (77 vs 82.1).
- The United States ranks last among our peers in healthcare access, measured by the number of deaths which could have been prevented by timely treatment.
- Post operative complications and medication/treatment errors are reported more commonly here than in most other wealthy nations. Sweden reports more treatment errors and Australia is worse on both counts.
- Our pregnancy-related statistics aren’t great either. The maternal mortality rate is nearly 4 times higher than the average comparable country. Doctors in the US perform more caesarean sections than other nations, and the rate of obstetric trauma during natural birth is greater here as well.
- There are some positives. The mortality rate among heart attack and stroke patients is lower in the US than in many other wealthy nations, and we also have lower rates of sepsis after surgery.

My family has had nothing but positive experiences with doctors and medical professionals, so these statistics surprised me quite a bit. Why do we spend so much on care despite substandard outcomes? There could be a number of contributing factors, including some which have nothing to do with the professionals actually administering care to their patients. One of these might be the fact that Americans, on average, don’t live the healthiest lifestyles. Furthermore, our mess of private health insurers may be making care more expensive than necessary. According to CBO data, Medicare is actually less expensive to administer than private health insurance, in no small part because of Medicare’s giant negotiating power. Whereas Medicare must negotiate with hospitals across the country, private health insurers often tend to have relationships with specific hospital groups or within specific geographic areas, limiting their negotiating power.

Nobody’s health care system is perfect and clearly ours has many great qualities. Medical centers like the Mayo Clinic and St. Jude’s Children’s Hospital are world-renowned. The US is home to many of the most advanced medical device and pharmaceutical companies, and we’ve all read stories of wealthy foreigners flying to the US to receive care from a medical expert because s/he’s the best in the world.

What I hope to suggest here is that we could all benefit from some civil discourse regarding our health care system, a subject which has always drawn strong opinions. Despite the fiery tone of rhetoric on both sides of the issue, I think most would agree our system could use improvement. Let’s come together with open minds to figure out how to make it better.

Sources: Peterson-KFF Health System Tracker KFF Medicare spending *Health Affairs* Medicare efficiency

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