Weekly Update

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- Quality stocks keep surging
- The market only cares about the top half of the K
- Housing is mixed, but steady supply and falling prices could finally bring pain
- Business surveys are mixed (and maybe useless)
- Leading Economic Indicators show signs of life
- China real estate in one chart
- Quick Hits
- Where did all the crypto money go?
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
S&P 500	4,869	2.7%	2.1%	23.0%
QQQ	$425.83	4.6%	4.0%	48.4%
US 10 YR	4.18%	4.11%	3.88%	3.50%
USD/DXY	103.3	103.4	101.3	101.8
VIX	13.1%	14.8%	12.5%	19.1%
Oil	$75.36	3.9%	4.8%	-6.3%

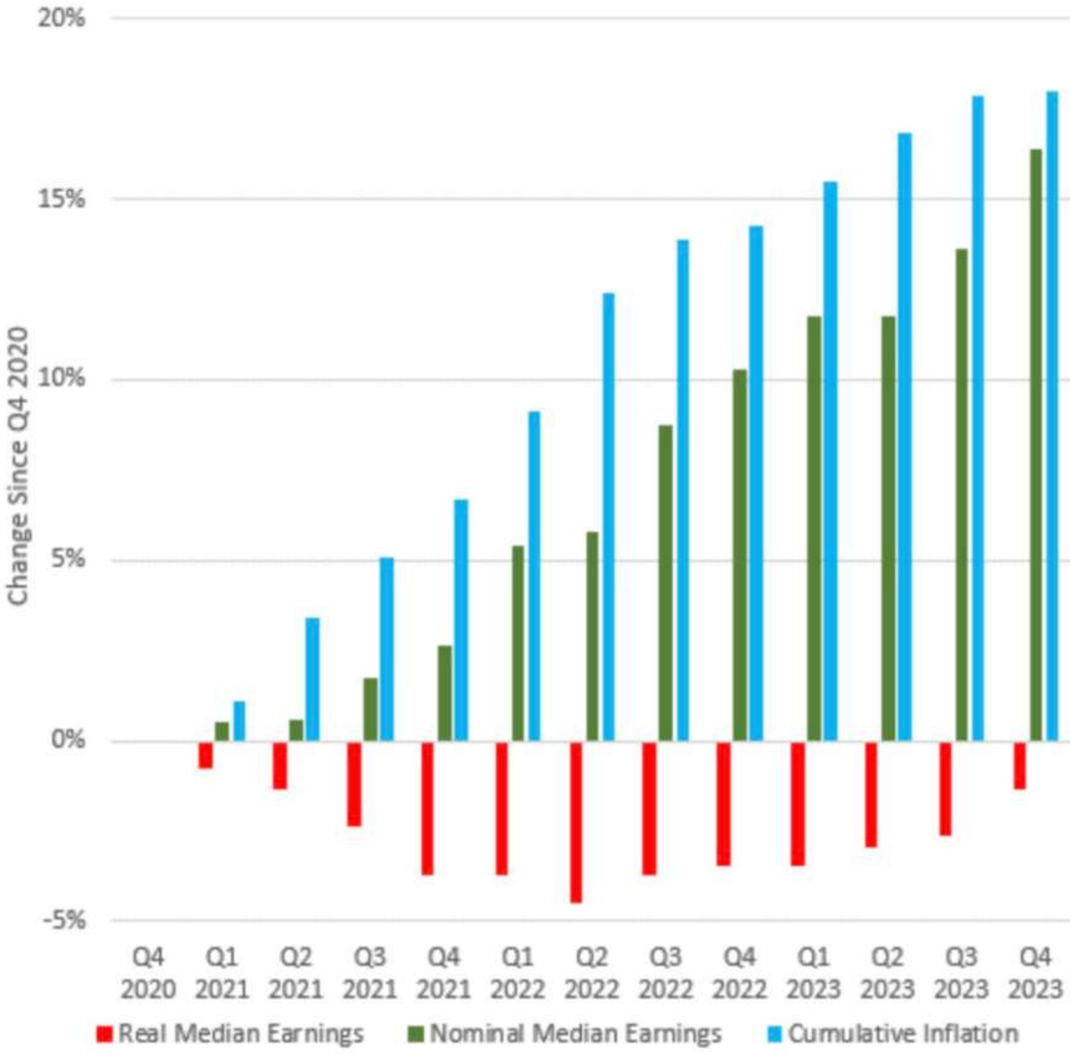
*10yr, DXY, and VIX are levels not changes
** Oil is front month futures, beware

Equities and bonds diverged this week. But it is the same pattern continuing to take shape: Large, Quality, profitable companies are doing well. Smaller, bad balance sheet, profitless companies are struggling. While Earnings season as a whole has been underwhelming so far, the upside surprises have been mighty. Obviously, Tech names have led the charge. With the increase in demand for computational power (a much better way to think about "artificial intelligence"), the companies that provide the means are in the catbird seat. But traditional consumer names are also exhibiting strength. From the usually staid Proctor & Gamble showing improving margins to Netflix having a huge surge in subscribers, the much-feared slowdown in the Consumer still seems off in the distance. There was even good news on the political front as Congress was able to extend the Continuing Resolution for another six weeks. Of course, that April 1 date at which point the budget will be automatically slashed by 1% is looming. And credit card debt is still a runaway train (along with a plethora of other warning signs including commercial real estate). But with the Fed about to cut rates (ex St. Louis Fed president Bullard thinks the Fed will cut rates way before inflation gets to 2%) and a likely end to Quantitative

Tightening (the Fed will resume reinvesting bond coupons and maturities), the market is happy to ignore its own overly enthusiastic rate cut expectations. All that said, clearly this is a momentum-driven market, and we know how that can turn on a dime. So we are not all-in by any means.

- The market only cares about the top half of the K

Before we sound too bullish, here is a chart showing the cumulative effects of inflation on the median income. It is still squarely negative with the lower half of the income scale (Wall Street types call this a K-shaped divergence) being punished disproportionately. Ultimately, Main Street's pain gets projected onto Wall Street. The bright side is that the rate of change of the negative real income is improving. Perhaps time will heal this wound, too.



Source: Bureau of Labor Statistics

- Housing is mixed, but steady supply and falling prices could finally bring pain

Housing Starts fell in December by 4.3% vs Nov. Building Permits ticked up a bit. Starts remain choppy while Permits are slowly trending higher. Existing Home Sales, meanwhile, continue to fall. The median price fell to $383k which is down 7.5% from the peak in mid-2022. Prices have dropped every month since June. Monthly supply increased to about 3.2 months which is good for a December number. This stat is the number of houses for sale vs the number being sold, so it is more a function of math (numerator flat, denominator down means result is higher).

Weekly Mortgage Applications increased again. The index is still about 75% below its peak across 2020-21. But lower rates are starting to turn the tide.

The optimist might say that housing is turning for the better. More houses are available, and prices are coming down slowly. The pessimist would list the exact same things.

- Business surveys are mixed (and maybe useless)

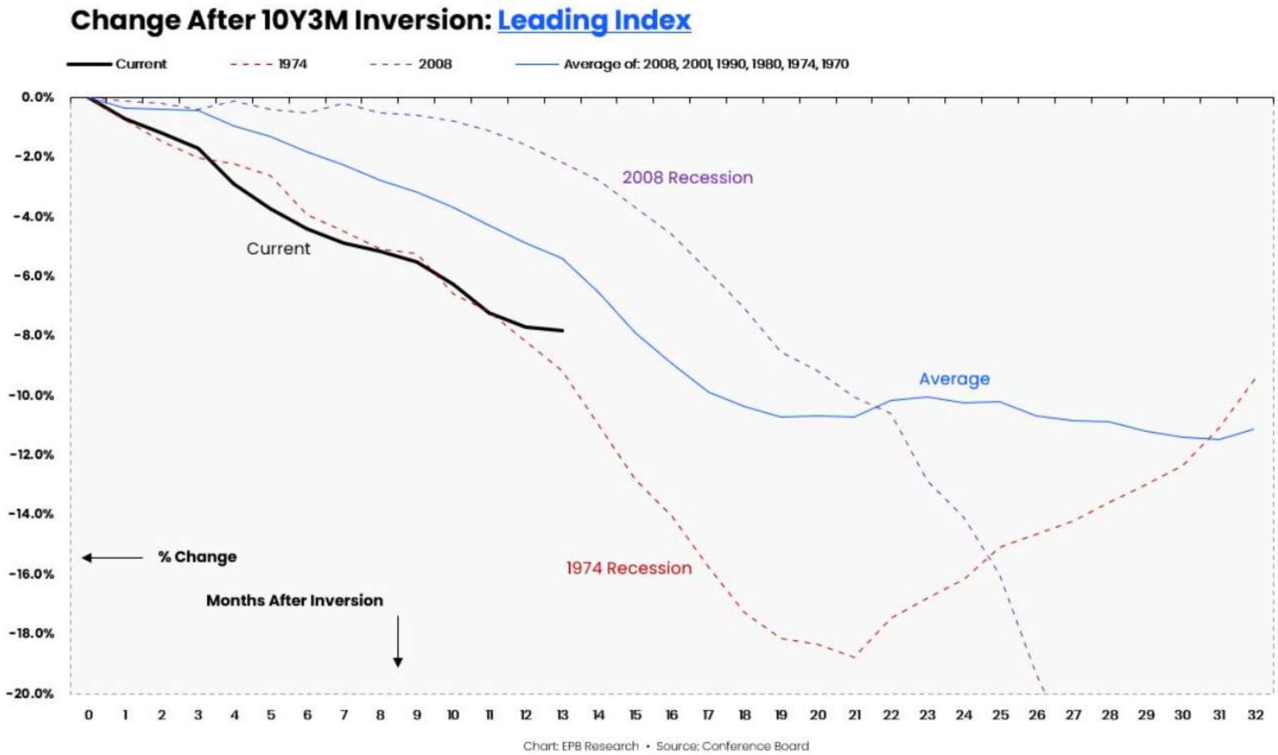
The S&P PMIs showed strength across the board in the early read for January. Manufacturing jumped about 2.4 points to get above the breakeven level (50.3). Services were already decent, and they moved another 1.5 points higher (52.9).

Philly Fed Manufacturing index stayed negative. It is not as disastrous as the NY Manufacturing (Empire), but that is not much solace. All subcomponents are negative except for Capex (which is similar to the sustained strength in Durable Goods Orders). The Richmond Fed's Manufacturing index slumped deeper into negative territory. But Services got a boost.

All of these various puts and takes just add to our skepticism of this data.

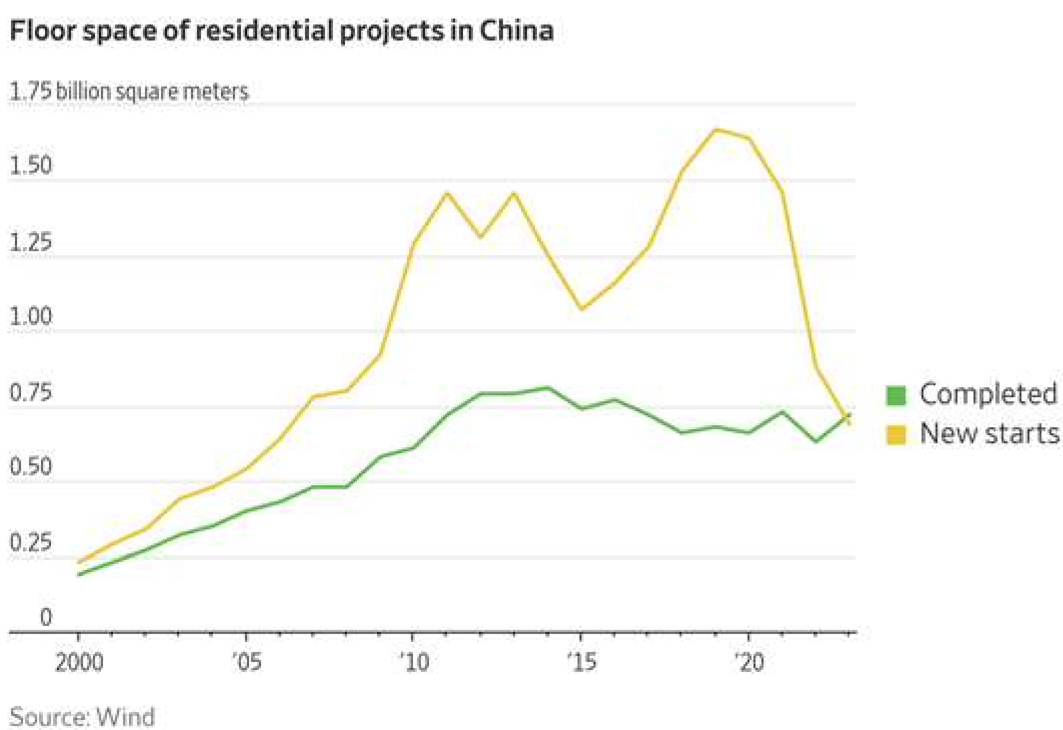
- Leading Economic Indicators show signs of life

The index of Leading Economic Indicators (December) fell for the 21st month in a row. However, it was the smallest decline in this period (-0.1%) and better than the -0.3% expectation. Six of the 10 components were positive which is the highest during this stretch. Stock Prices were the largest contributor on the plus side. The ISM New Orders survey was the largest on the downside. As we have stated, we have lost quite a bit of faith in the business surveys (business managers simply are not doing what they say they are doing or intend to do). The chart below (from EPB Research, a good Twitter follow) shows that the LEI index usually starts to accelerate to the downside a year after the yield curve inverts. But the current index appears to be leveling off or at least not worsening. Obviously, the sample size is laughably small, and the recent divergence is slight. We shall see if this trend holds.



➢ China real estate in one chart

Here is a great chart from the WSJ that encapsulates the ongoing problems with the Chinese real estate market. Instead of bridges to nowhere, it is houses for nobody. (And we are slightly perplexed by the WSJ's source, "Wind.")



- Other data is positive

Redbook Retail Sales increased 5.2% on the week. This 4%-6% level (last 5-6 months) is roughly the pre-Virus Fear level. Of course, this data is not adjusted for inflation.

Michigan Consumer sentiment jumped again for the second straight month. This is the survey based on inflation. The 5-year expectation is down to 2.8%.

- Where did all the crypto money go?

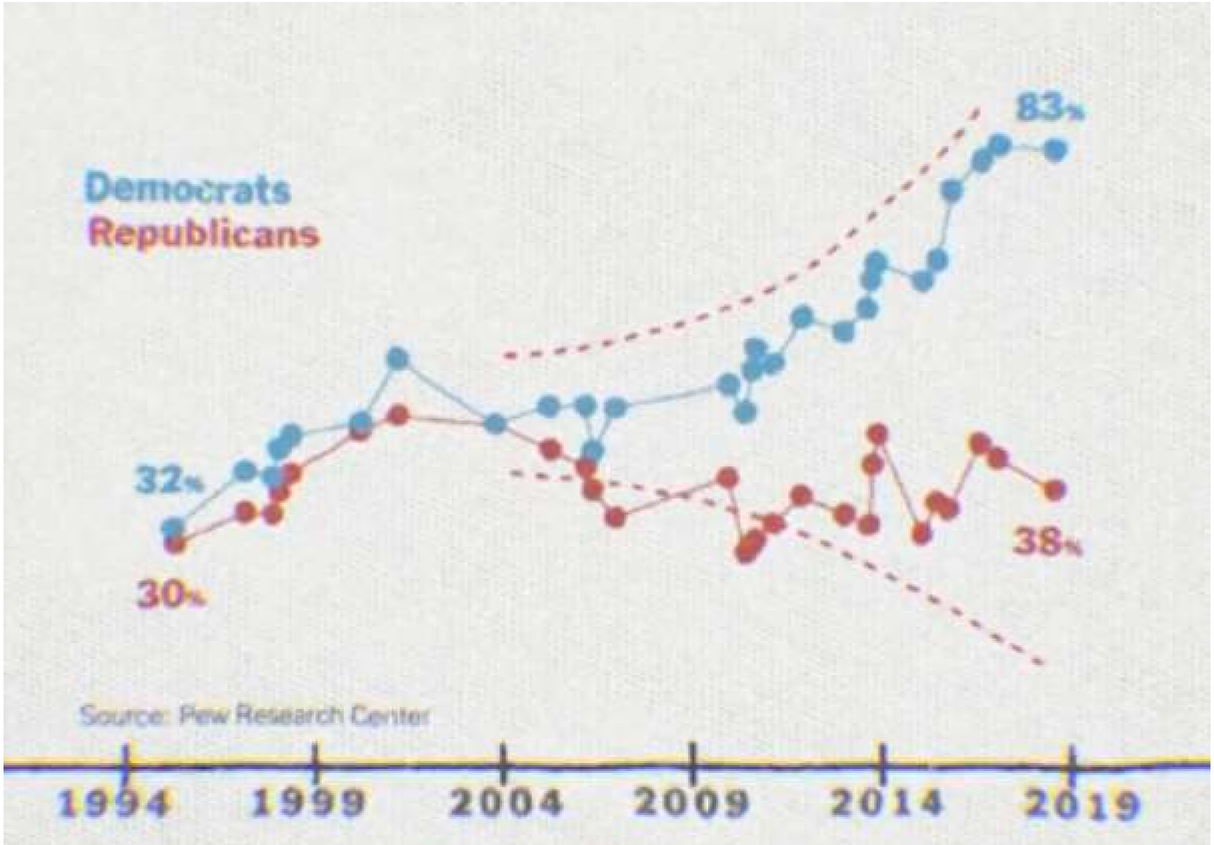
Every time we think we have run out of stories to tell about crypto (it is inherently worthless, you can make a lot of money trading it, blockchain has potential, NFTs could benefit the art world, and do not fall for the scams), more craziness is exposed. And this one is pretty high on the list:

USI Tech was an "investment plan" launched in 2017. The founder, Horst Jicha, had a simple pitch: He would make you 1% a day every day for 140 days. He broadly spoke about buying Bitcoin and crypto mining and "algorithms" without any explanation. But wait, there is more. Current investors in the scheme were offered commissions to recruit new investors in the scheme! When he was asked if this was a Ponzi scheme, he answered, "Now you might be thinking this is too good to be true." Well, when Jicha received multiple cease and desist letters from various regulators across the US and Canada (for selling unregistered securities etc), he simply vanished with the $150mm from investors. This story came to light a few weeks ago when Jicha returned to the US to vacation in Miami. Just like Hyman Roth, the Feds were waiting for him. Fortunately for Jicha, Rocco Lampone was not.

And GameStop is shutting down its NFT marketplace because it is worried about "regulatory uncertainty." Maybe they watched Horst go to jail!

- Chart Crime of the week

The title of this chart in the New York Times was, "Things Fall Apart: How the Middle Ground on Immigration Collapsed." We guess telling us what the data was also fell apart. And even if it were real data, that red trend line (the dashed line) is more than dubious.



- Quick Hits
    - Sports Illustrated is going out of business…sorta. The magazine has been under a license agreement between two companies…one that owns the brand and the one that publishes it. The one that publishes it is being taken over by the guy who started 5-Hour Energy. Before he bought the whole company (there is still a pending tender offer), he decided to buy stock and bonds of the company in the market. He accumulated enough stock to fire the board of directors putting himself in control. He stopped paying the licensing fee to the owner of the SI brand, and then he fired all the staff of the magazine. To recap: 5-Hour Energy guy paid a lot of money to buy the rights to a brand and then he terminated his rights to the brand.
    - Joey Gallo struck out 42.8% of his plate appearances last season with a .177 batting average.
    - North Dakota is the third largest oil-producing state.
    - The WWE (pro wrestling) bagged a 10-year $5b distribution contract from Netflix.
    - The head of Southwest's flight attendants' s union is upset that the airline "does not value employees equally." She was referring to the different contracts offered to pilots.
    - Dean Phillips, the only democrat challenger to Biden, won 20% of the vote in the NH primary. He will get zero delegates.
    - Adrian Beltre had a hit off 9% of all the players to ever throw a pitch in a MLB game.
    - A California woman was arrested for stealing $2500 worth of Stanley drinking tumblers. An arrest in California is the real headline!
    - A Californian congressman, Ted Lieu, is introducing a bill to ban pest glue traps.

Trading: We sold the balance of our long Japanese equity / short Yen (long USDJPY) position. Even though the Bank of Japan kept interest rates negative, Ueda's (head of the BOJ) comments point towards a tightening sooner rather than later. And economic data continues to be weak. We would rather get out ahead of the market turning on this good winner. We added a small bit to our long in India. Unlike Japan, it has accelerating economic data. There was a brief hiccup this week as "profit taking" swept across the market. We will take these days to add to one of our favorite markets. We still do not want to be too large. It is, after all, an emerging market. We have a few new names we want to buy (Tech, Media, Pharma), but we want to see some weakness first.

TSLAQ: Tesla Earnings disappointed. Gross margins and operating margins both declined and fell short of expectations. Basically, the price reductions have been hurting as expected. Looking ahead, Tesla is not providing revenue guidance, but it will fall short of 2023's growth. Hopefully there will be some Elon fireworks during the conference call (one salient point is that margins are not going to improve, but we need to review this in its entirety later).

Of course, earlier in the day before the earnings release, Tesla leaked a story to Reuters about a new "mass market vehicle" getting ready to launch. Supposedly Tesla has told suppliers to get ready for mid-2025 which would mean a 2026 launch. Alas, Tesla has never hit a production launch (or enhancement launch). Tesla should probably try to miss this launch as all it will do is cannibalize its model 3. And if the new "Redwood" model (not its name, but the code name for telling suppliers to get ready…good lord) really is going to be ~50% of the price of the model 3, Tesla shareholders might not want this margin killing machine come to light. Tesla did announce that it would be revolutionizing auto manufacturing blah blah blah. What we know is that Tesla took a Honda Civic and broke it down to see how it is put together. True story.

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