Weekly Update

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- Death Rotation is back
- Earnings are strong, but will the reactions be?
- Economic data is not dipping
- Fed leaves interest rates at 0%, will they ever change? (hint, no)
- The White House assault on oil & gas is mostly political bluster
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
SPX	3751	-2.6%	-0.1%	16.0%
QQQ	319.4	-1.3%	1.8%	44.5%
US 10 YR	1.03%	1.08%	0.92%	1.66%
VIX	37.2%	21.6%	22.8%	16.4%
Oil	52.85	-0.8%	8.3%	-1.2%

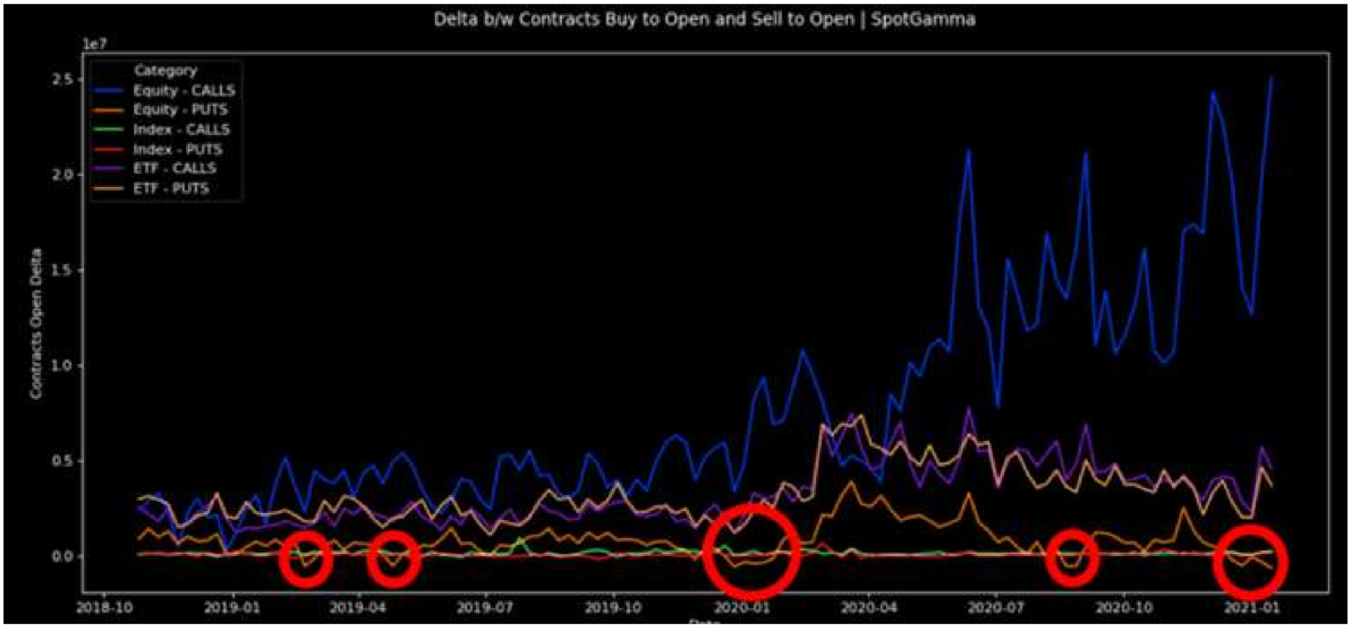
*10yr and VIX are levels not changes

** Oil is front month futures, beware

The Death Rotation is back! The GameStop mania is reverberating throughout the marketplace. For those fortunate enough not to have to hear/read about this trading phenomenon nonstop, here is the one-liner: the stock market is squeezing heavily shorted stocks higher which results in hedge funds with these short positions having to cover them and sell their unrelated long positions. This “de-risking” or “de-grossing” results in other funds having to do the same thing. Even funds without any exposure to the crazy names decide to rush to the exits before someone else is forced to capitulate. The headlines may be reading that the Reddit message boards are driving the market…that is just an entertaining sideshow. On top of some hedge funds unwinding their positions, there is also a swath of hedge funds that are forcing these unwinds by chasing the crazy side of the trades! Even Chalk Creek has gotten in the on the action! We suspect this kind of trading activity can persist for a few weeks with more than a few head-fakes. Whatever the timing may be (fool’s errand trying to call that), we will know we have reached the bottom when the chest thumping, finger wagging, and rocket emojis have vanished from the “front page of the internet.” (That is what Reddit unabashedly calls itself.)

As for the real world, the negative narratives seem to be creeping back. Someone in China apparently did not get the communist memo: virus cases are climbing, and lockdowns are being reintroduced. The stimulus in the US is getting some pushback from moderate Repubs. On this note, Senate Repubs have negotiated a power-sharing deal with the Dems. Obviously, the Dems still have the real power, but Repubs will hold an equal number of seats on the ever-important committees. And market positioning is still running hot. Retail investors’ s allocation to equities is at an all-time high (not talking about just the ‘Hooders but all Retail). Market

Shorting is near its all-time low (everyone has thrown in the towel on their hedges as SPY shorts are now about 1% vs a five-year average of 4%). And the options market is heavily skewed towards Calls. This chart (courtesy of The Market Ear…we need to tell them to enhance their graphics) is a bit in the math-weeds, but the point is that the blue line shows how volumes on single-stock Call options have exploded. Moreover, the market is actually short Puts! (Actually, the market is technically always neutral all options because there is a seller for every buyer, but the market can tell which side, the buyer or the seller, initiates the trade.)



- Earnings are strong, but will the reactions be?

It is still a little early in the earnings season with just less than 25% of the S&P 500 having reported. But so far, 87% of companies have beaten EPS expectations and 78% have beaten revenues expectations. These are phenomenal percentages. And as we have written, expectations have been climbing into the numbers. Alas, the market might expect more than the official expectations (sounds silly but vey common). So far, the correlation between strong earnings and strong market performance is low. This analysis is likely to break down even more as the market rotation and macro direction are exerting their force. The FATMAN stocks are reporting this week (so far, very strong numbers ex Tesla…shocker), so we will see which force is dominant. Here is a snapshot showing the increase in earnings expectations. The actual EPS growth so far (the 25% having reported) is +1.5%.

Sector	Today	1 Jan	1 Oct
Consumer Discretionary	-21.7%	-22.6%	-25.9%
Consumer Staples	3.3%	-0.5%	-2.1%
Energy	-105.3%	-98.3%	-86.7%
Financials	17.5%	-6.6%	-22.1%
Health Care	5.2%	3.4%	4.3%
Industrials	-45.9%	-41.7%	-40.0%
Materials	9.3%	6.1%	-2.1%
Real Estate	-11.5%	-11.9%	-12.5%
Technology	11.5%	3.7%	2.8%
Communication Services	-11.0%	-12.5%	-17.9%
Utilities	-2.4%	-3.0%	-2.7%
S&P 500	**-4.3%**	**-10.3%**	**-13.6%**

- Economic data is not dipping

We have recently noted that economic data is starting to slip…at least vs expectations. While still at good levels (ex-Unemployment), a slipping trend could be worrisome. Well, Housing, Business Surveys, and Business Spending all look pretty strong in the latest round of data.

New Housing Starts and Permits accelerated in December to reach the levels of 13 years ago. Existing Home Sales are doing even better as they are almost back to the all-time high seen during the 2005 Housing peak. The Northeast had the strongest growth while the West lagged. Inventory of homes for sale is still just 1.9 months of supply (a record low). The average number of days that a house sits on the market is down to 21. And foot traffic in December was +24%...so the trend is likely to keep going. The median price was $310k. This is still sitting near the recent high. Pricing has been a worry…that these high prices would start to depress demand. But the opposite is happening. High-end homes are selling while homes under $100k are barely moving. This is another unfortunate byproduct of the government shutdowns – forced unemployment has hit the lower-end of the economy much more severely (Jobless Claims are starting to tick higher).

Of course, a huge boon to the Housing numbers has been forbearance. The idea behind allowing people to not pay their mortgage payments on time was to do just that - bide some time. And this worked throughout the summer and fall as the share of mortgages in forbearance dropped steadily from 8.5% to 5.5%. But now forbearance has leveled off. Apparently, (we qualify this because we do not have the source other than a ZeroHedge tweet), 20% of all renters are behind on their rents to the tune of $57b. This is one of the most important data points / government policy positions to watch (another bailout coming, no doubt).

The early reads on the January Markit PMIs were strong. This is true for both Manufacturing and Services. We have been focusing on the increase in Manufacturing to keep the economy going while the vaccine rolls out. But if Services are already picking up? That is great news. But the regional Fed surveys paint a more mixed picture. And it does not include the same regional biases we have seen recently – but rather the opposite. Both Dallas and Richmond showed drops in activity optimism while Philadelphia surprised sharply to the upside. These moves are on the margin, and we expect them to revert to the trend.

Durable Goods in December only showed a slight uptick on the headline Orders number. But the Core Capital Goods number…aka Business Spending… showed a nice boost along with an upward revision in November.

- Fed leaves interest rates at 0%, will they ever change? (hint, no)

The Federal Reserve's Open Market Committee obviously left rates unchanged at 0% (technically its target for the Fed Funds rate which is the rate at which banks lend to each other) and left its bond buying plan intact. Given the recent emphatic messaging from the Fed leaders, we know nothing is going to change any time soon (and the futures markets agree with 100% certainty…yikes?). This is the primary reason for our still bullish outlook in the short to medium term (notwithstanding the ongoing rotation in the immediate-term and the insane debasing of the dollar and our debt in the long-term).

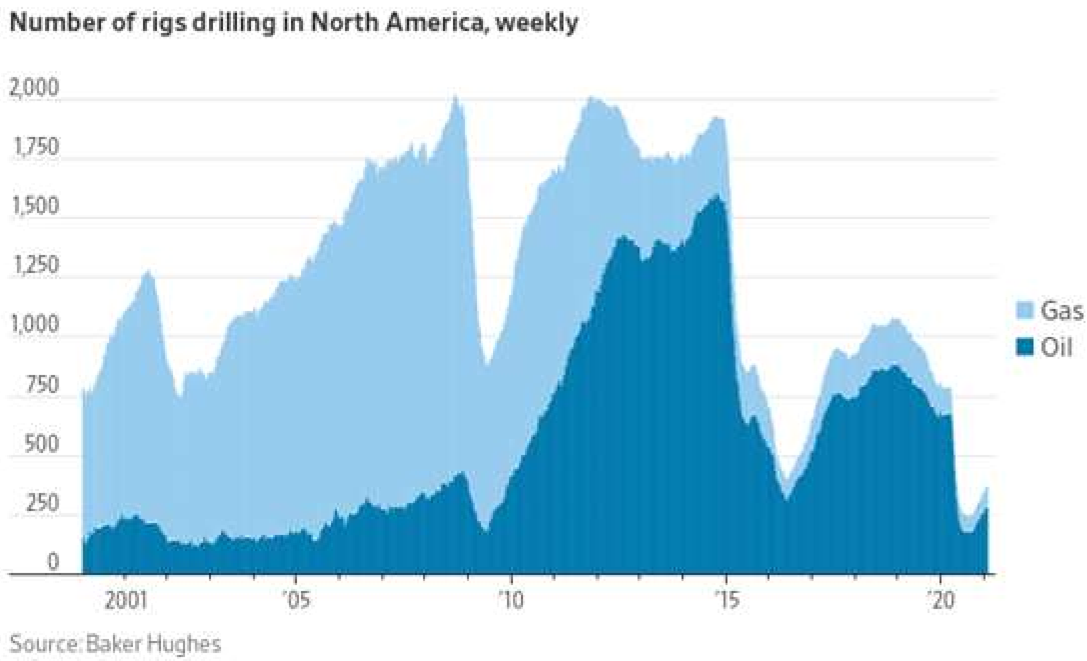
Moreover, Jerome Powell continues to step outside the bounds of the traditionally apolitical Fed role. That is, the chair has moved on from simply advocating for more fiscal policy to proactively pushing social policy. Of course, the irony of the "we must social distance" narrative was lost on Powell while he was describing the hardships forced upon the lower-end Service workers.

Powell went on to say that he thinks the migration theme out of the big and dirty cities (dirty is our word) is only temporary and that the recent spike in housing prices (and thus their input prices like lumber) will cool. He conveniently left out the Work-From-Home theme which is also playing a large role in Housing. And we think he is wrong about the migration theme.

Powell finished his press conference with some other doozies. He acknowledged corporate debt is potentially in bubble territory, but the Fed is just watching and cannot do anything about it. When asked about the permanent damage to the job market, he demurred and said, "the jury is still out," and that it depends on the virus. Our point is not to bash Powell but rather to highlight his insistence on his way being the right way. In other words, interest rates and bond buying are not going anywhere.

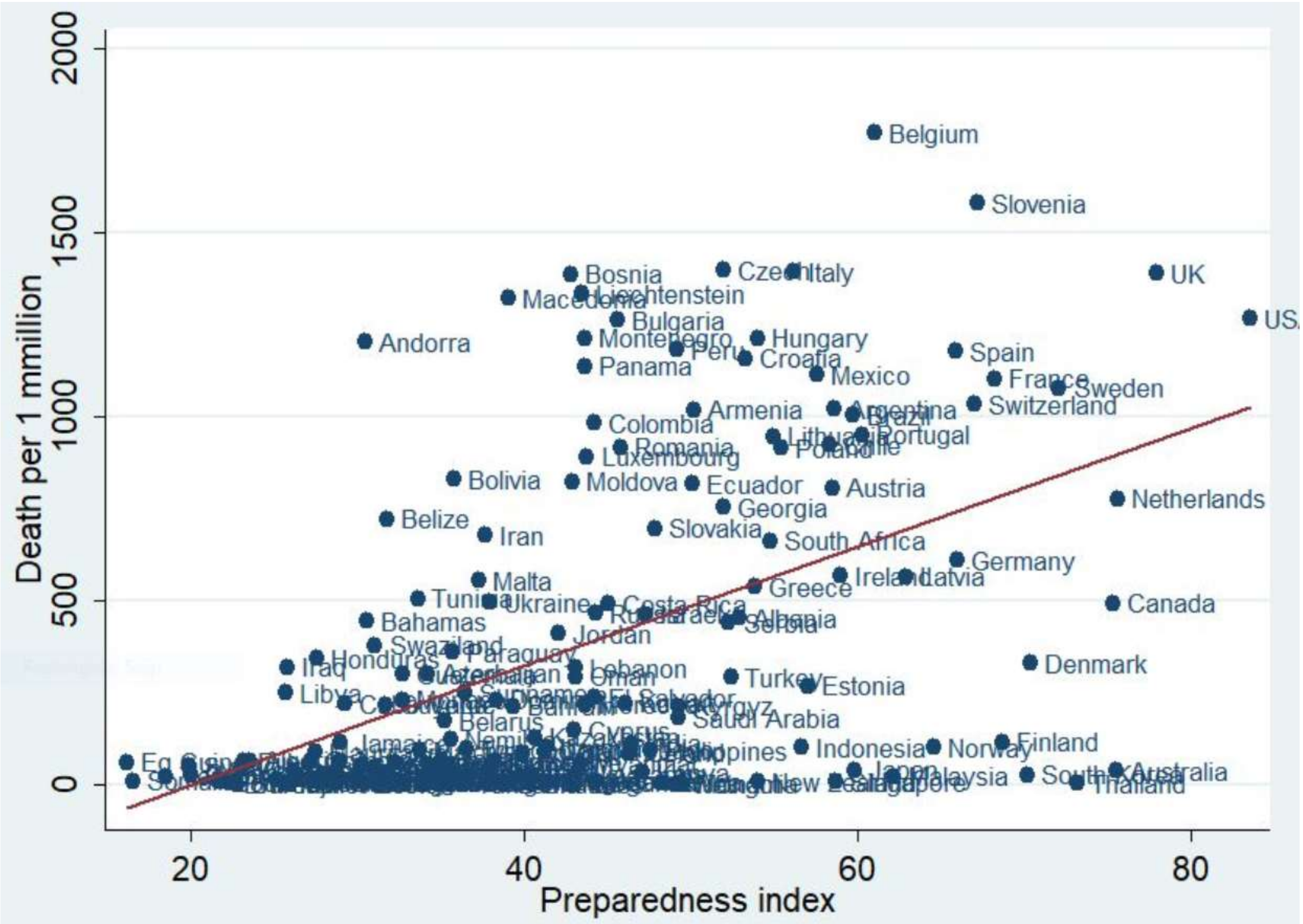
- The White House assault on oil & gas is mostly political bluster

The media is circling the wagons on the oil & gas industry as Biden halts new drilling permits on federal land. A few things to keep in mind beyond the headline: Drilling on federal land only accounts for 9% of US production (onshore), most oil companies have stockpiles of permits so they can continue with new production leases for years to come, and the overall level of drilling activity is already incredibly low. We do not necessarily think broad investments in the oil & gas industry make a lot of sense right now…the government can still make your life miserable. But we also do not think discounting the entire industry is wise. The Dems assault on Energy will have plenty of unintended consequences which might be investment worthy (killing some pipelines will benefit others, killing permits will increase the price of oil, incumbents can squash smaller rivals, etc).



- Chart Crime of the week

We will skip the low-hanging fruit of the GameStop world…we cannot take it. So, we will shift to a virus chart. These tend to be more laughable anyway.



- Quick Hits
  - A GameStop dedicated “research” website is using a multiple to value the stock based on Ryan Cohen’s dog. We have no idea what this means. But they are serious.
  - In the latest blockbuster UFC fight, the loser won $5mm and the winner won $1.05mm (these are salaries and bonuses before their cut of the pay-per-view which will skew these numbers even more).
  - The Miami Heat (NBA) will use virus-sniffing dogs at its home arena.
  - Valentine’s Day *cards* are being quarantined for seven days this year at schools.
  - In 1998 and 1999, if a company added “.com” to its name, the stock would rally (on average) 74% over the next 10 days.
  - The San Francisco public school named after Abraham Lincoln is changing its name for the horrible grievances directed at Indians (apparently).
  - Current US Senator Diane Feinstein is also being stripped of her glory. The public school named in her honor is purging her questionable history. She once repaired a confederate flag that flew outside of city hall when she was mayor in 1986.

Trading: We have a few distinct views on trading right now. 1) Since we believe this Death Rotation will be short-lived, we are looking to add to names that get swept into the “de-risking” for no fault of their own. These include our Healthcare and Big Tech names. Our long Financials position is small: we have been waiting to add as they are retracing from their run into strong earnings. This could be the right time. 2) We have cleaned up some of our short-term trading names. We sold the last bit of our GameStop (lightyears below the current levels). We exited our Blackberry with a nice gain. We have orders to sell some of our squeezing retailers, but we are riding those a bit longer (got trapped buying one near a dumb spike, oops). We still have some of our crazy EV names which are rocking. We might have to cut these in order to reload lower. 3) Even though we have been pretty diligent in cutting our long exposure during the last few weeks (cutting more Big Tech than what we bought in the High Growth high-fliers) including adding some Put protection, we will look to do more of this on any sort of upticks or calm days. In general, we might look to increase our exposure to the Recovery trade (vs Lockdown) as the Fed is still hell bent on inflating the stock market (they would say "the economy"). And the physical reopening of the economy will obviously face less resistance from the powers that be now that they are the powers that be.

TSLAQ: Nary a mention of Tesla all week in the financial media! In fact, Musk felt so shunned from the spotlight that he had to tweet about GameStop. One could argue that this tweet caused another leg up in the stock as his fanboys joined the Reddit maniacs (aka the quant hedge funds who are using Reddit as cover). And oh yeah, Tesla reported lousy earnings. The Villains fantasy world conference call is tonight, so we look forward to a few good laughs.

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