Weekly Update

29-November-2023
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- Equities are following the soft-landing narrative, bonds and oil are not
- Maybe China is not the next foil
- Credit card delinquencies and charge off trends depend on the borrower
- Positioning is high strung
- Earnings have been better but revenues have not
- Interest rates matter more for small caps (cont.)
- Decent Black Friday shopping vs a low bar
- Housing data is mostly negative
- Leading Indicators are screaming for help
- Business surveys for Manufacturing are getting worse
- OPEC production cuts are likely to outpace Russia sanctions
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- Where did all the crypto money go?
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
S&P 500	4,551	-0.1%	19.8%	16.6%
QQQ	$389.81	-0.1%	47.0%	38.8%
US 10 YR	4.25%	4.41%	3.75%	3.61%
USD/DXY	102.8	103.9	104.5	106.0
VIX	13.0%	12.9%	22.9%	20.6%
Oil	$77.62	0.7%	-3.3%	-0.8%

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

Different asset classes are signaling the same thing about the direction of interest rates: Lower. But the reasons behind this consensus are polar opposites. Equities are just shy of all-time highs because the soft-landing (or no-landing) narrative is firmly in place. Never mind the economic data, the warnings from Walmart and Target, maxed out credit card debt, turmoil around the world, etc. All that matters to equities is that market interest rates are going lower. But this rally in the bond market is *directly* a result of this bad data. The market is anticipating the Federal Reserve having to cut interest rates to stave off a recession. The oil market, which has been more right than other asset classes in recent years, has been signaling economic weakness ever since the data started rolling over (late summer). And as we have been repeating, non-emergency rate cuts are bad for equities! But until that realization sinks in, the "what have you done for me lately" market will sustain itself. Of course, it is plausible that the market thinks the Fed can eradicate inflation without hurting the economy. We also think this is plausible. Although it would be the first time ever. What we really need to watch in the medium term is the government's funding plans. The reduction in the supply of long-term bonds has helped propel the markets higher (bons and equities). If auctions start to wobble (the much watched 20-yr auction* was a success with a better yield with more non-dealer demand), this recent momentum rally could fade. And lest one doubt the momentum of this market, it only took 16 days to recoup the 10% drawdown that hit in October. That was the quickest market recovery in over 50 years.

That said, our base case is still for mild economic weakness through which the large, Quality companies can survive if not thrive (rich get richer).

- Maybe China is not the next foil

We have repeatedly included the growing rift with China as a non-zero risk (for the economy, markets, peace, you name it). Naturally, Xi's trip to meet Biden in San Francisco had the eyes of the world focused. Alas, not much came of this meeting. Of course, this was never about politics but rather it was a business lobbying effort by Xi. Without any self-awareness, the media reported Xi kissing ass to Schwartzman and Fink (the CEOs of Blackstone and Blackrock who are quick to virtual signal at home but not so much abroad) while they fawned over their communist hero. The relevance is that Xi needs the US maybe more than we need them. And as for the health of the Chinese market, the communists have banned any large owners (5%) from selling any stock. Schwartzman and Fink have not commented.

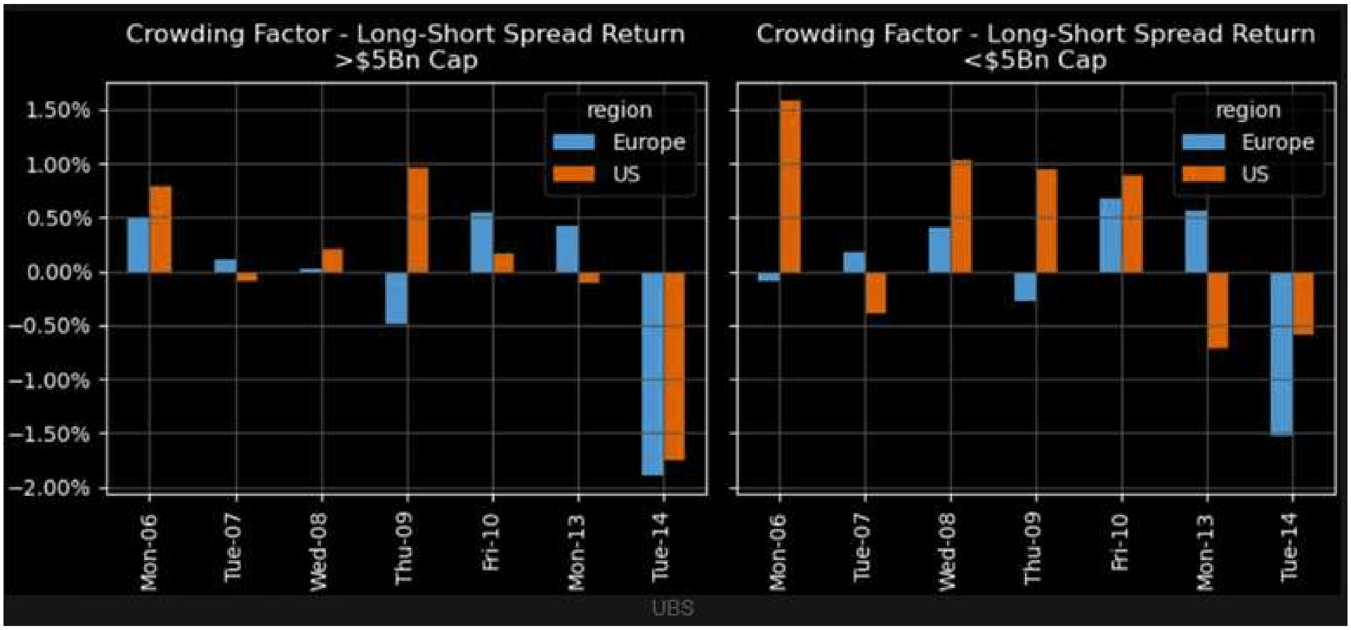
- Credit card delinquencies and charge off trends depend on the borrower

We have been increasingly talking about the tenuous state of the consumer. The latest credit card data for October supports our theory that there is a tale of two worlds. While average delinquencies and charge offs are up in Oct 2023 vs Oct 2019, the good banks have stable if not better metrics. The lower quality lenders are rapidly deteriorating. (If the last column is positive, ie Capital One and Discover, that is bad. If it is negative, JPM and Citi, it is good.)

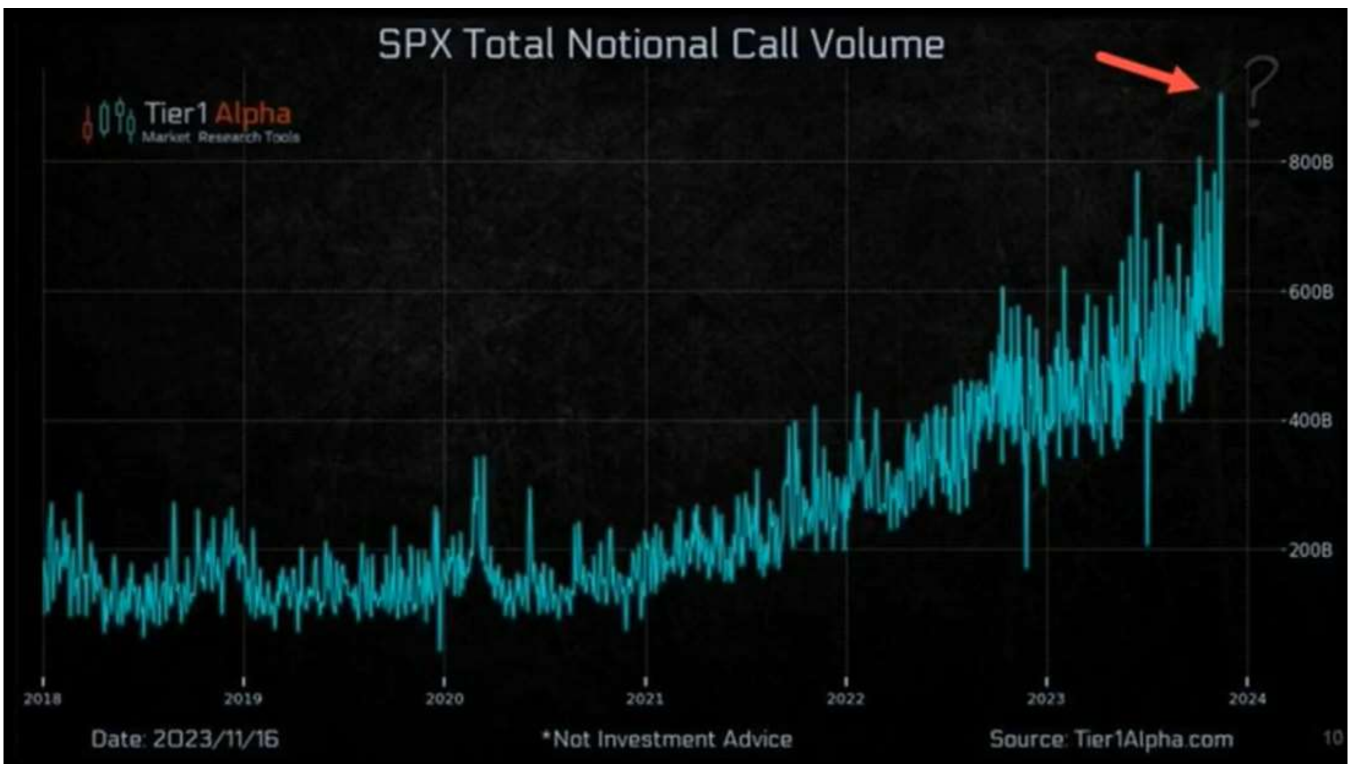
			2023					Change in bps
Company	Ticker	Type	Oct.	Sept.	Aug.	3-month average	Oct. 2019	(Oct.'23 vs. '19)
Capital One	NYSE:COF	delinquency	4.48%	4.31%	4.09%	4.29%	3.79%	69
		charge-off	5.08%	4.16%	4.55%	4.60%	3.95%	113
American Express	AXP	delinquency	1.30%	1.30%	1.20%	1.27%	1.60%	-30
		charge-off	1.90%	1.70%	1.70%	1.77%	2.30%	-40
JPMorgan	JPM	delinquency	0.98%	0.95%	0.90%	0.94%	1.16%	-18
		charge-off	1.65%	1.60%	1.68%	1.64%	1.61%	4
Synchrony	SYF	delinquency	4.60%	4.40%	4.10%	4.37%	4.50%	10
		adjusted charge-off	5.60%	4.40%	4.70%	4.90%	5.10%	50
Discover	DFS	delinquency	3.61%	3.41%	3.15%	3.39%	2.58%	103
		charge-off	4.42%	4.15%	4.16%	4.24%	3.27%	115
Bread Financial	BFH	delinquency	6.50%	6.30%	5.90%	6.23%	5.90%	60
		charge-off	8.00%	6.70%	6.70%	7.13%	6.60%	140
Citigroup	C	delinquency	1.39%	1.33%	1.28%	1.33%	1.58%	-19
		charge-off	2.07%	2.13%	1.97%	2.06%	2.61%	-54
Bank of America	BAC	delinquency	1.37%	1.30%	1.26%	1.31%	1.62%	-25
		charge-off	2.06%	2.11%	2.13%	2.10%	2.41%	-35
		Avg. delinquency	3.03%	2.84%	2.68%	2.85%	3.18%	19
		Avg.charge-off	3.85%	3.26%	3.35%	3.48%	3.48%	37

- Positioning is high strung

We have recently lamented the declining value in positioning data. Without going into the latest contradictory points, we saw a new one that was telling. UBS shows that the performance between crowded longs and crowded shorts exploded to the downside two weeks ago. This is a tiny sample size. But it illustrates the high-strung nature of this market; short squeezes are violent. We would add that when the squeezes calm down, they do not really deflate. But rather, the Big Tech (and other non-short squeeze favorites) grinds higher to catch up. This is anecdotal at best, but it does support this being a momentum driven market.



And Tier 1's chart showing the latest burst in Call option buying (in an already upward sloping curve) reinforces this mad scramble to get right-footed.

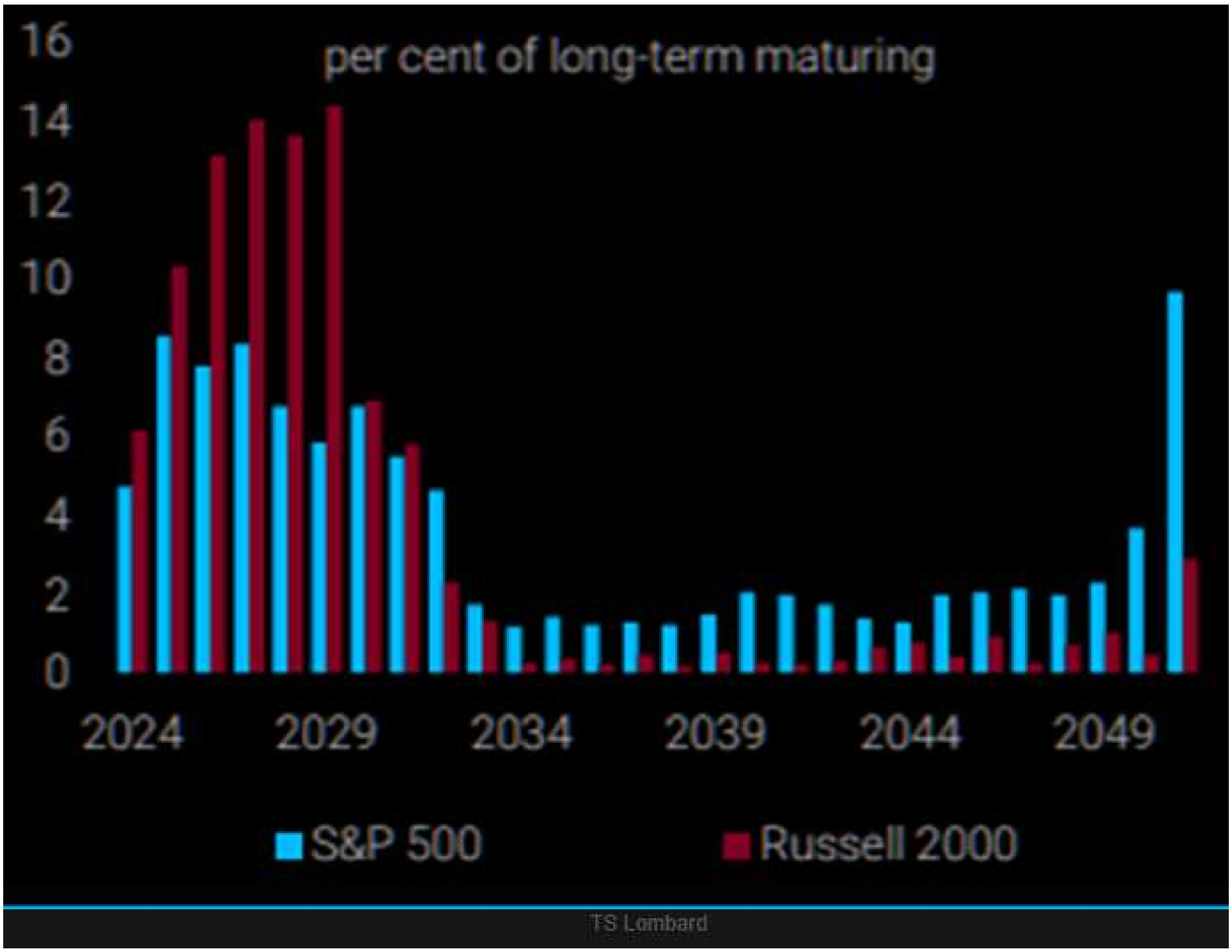


- ➢ Earnings have been better but revenues have not

Earnings season is over 95% done. Earnings per Share have grown about 6.6% on a blended basis (reported and estimated for the small balance of companies yet to report). Revenues have grown about 1.4%. This sums up the tale of the tape. Companies have done a good job trimming the fat (or just getting lucky with input prices falling), but Sales are barely growing. Top line growth is paramount for future Earnings growth (you can only squeeze so much juice out of costs). Earnings growth is expected to dip a touch in 4Q (down to 5.6%) and then reaccelerate in the next two quarters (7.7% in Q1 and 11.4% in Q2). Meanwhile, GDP is likely to slow according to the NY Fed and other professional guessers. We know these numbers (Earnings and GDP growth) are not always in sync. But the dislocation in expectations seems extreme.

- Interest rates matter more for small caps (cont.)

We have laid out the difference in interest rate sensitivity between different sized companies before…small caps have effective interest rates almost triple that of large or mega caps. Importantly, these same small caps (Russell 2000) have more debt coming due in the near future.



- Decent Black Friday shopping vs a low bar

Mastercard reports that Black Friday spending increased 2.5% vs last year. Online spending supposedly hit a record of $9.8b which is an 8.5% increase. Brick & mortar spending increased 1.1%. None of this is adjusted for inflation. In early September, Black Friday Sales total sales were expected to rise 3.7% (we do not know how or why Mastercard tries to pinpoint this). Online did better (6.7% expected) and stores did worse (+2.9% exp).

Also, Shopify, the behind-the-scenes platform that runs the e-commerce businesses for smaller companies, saw its Black Friday sales increase 22%. (Shopify does have an instore platform for businesses, but this data is not included).

Generally, discounts drove the increase in sales. And expectations were beaten down enough (Walmart and Target were two that warned of a weakening consumer) for a ”surprise” to materialize. We still think the consumer is not as strong as the pundits believe (there was a surge in buy-now-pay-letter which mostly means traditional credit tapped out).

- Housing data is mostly negative

The Housing Market Index (aka the homebuilder survey) fell sharply again. It is heading back to the Virus Fear lows. All three subcomponents exhibited weakness (Current Sales, Expected Sales, Buyer Traffic).

Housing Starts and Building Permits in Oct both increased and beat expectations. Permits are trending better than Starts…and obviously Permits are leading. Recently, we noticed that the two were diverging without any follow through from Starts.

New Home Sales in October slumped 5.6% vs an increase of 8.6% in September. And prices are slumping, too. The median price was $409k which is down 18% vs last October. Of course, this is still up over 23% from the pre-Virus Fear level of $332k. The peak was $497k a year ago October.

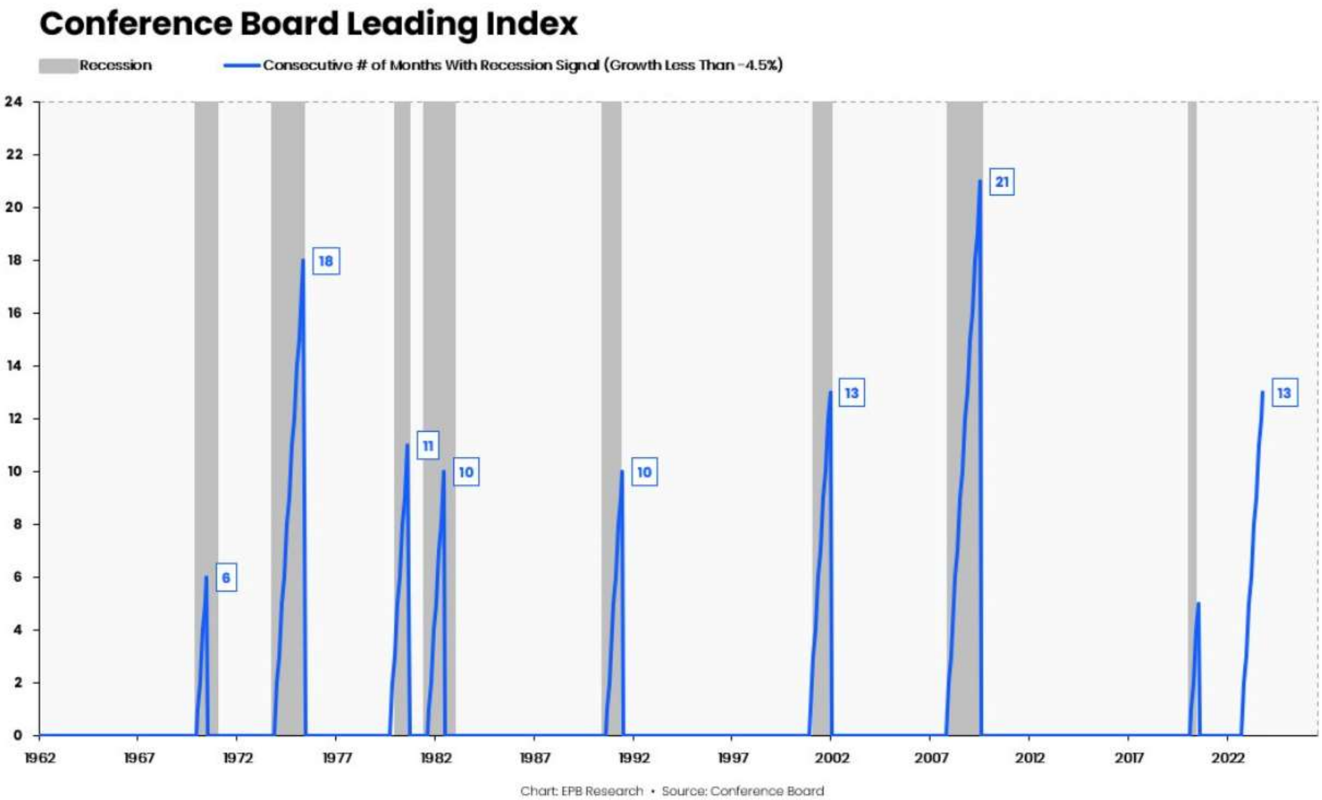
Existing Home Sales fell to their slowest pace since August of 2010 when the homebuyer tax credit expired (a few months before this). The annualized number dipped to 3.79mm in October from 3.95mm in September. This was the largest monthly drop in a year. Supply did tick up almost 2%. But it is still only at 3.6 months (and this calculation uses the current sales number, so the gross number of homes for sale is still low). The median sales price was $392k which is an all-time high for October. The market is split with lower end homes seeing strong demand. There is more supply on the higher end of the market along with more price concessions.

Mortgages Applications during the last two weeks ticked higher for the third/fourth straight weeks.

Tying it all together: Builders are nervous. Permits have been increasing, but the lack of follow-through form Starts and the downturn in Sales are more meaningful. The use of incentives is still supporting the market. Existing Homes are barely moving even with the slight reprieve in interest rates. We think this data reflects our view of the economy. Weakness is likely on the horizon, but it probably will not be bad enough to break the market. We do not have any direct exposure at this time (waiting to buy a dip).

- Leading Indicators are screaming for help

The Leading Economic Indicator index for October declined again. This brings the streak to 19 months. The Conference Board, the creators of the index, has a recession signal which is marked by the index falling below -4.5%. The index has been below this level for 13 months now. Some armchair quarterbacks on Twitter point out that there are other Leading Indicator models that are not showing weakness. Fair enough. All models are fallible. But this one seems to have a pretty strong track record (we picked this from EPB Research which has some good Twitter stuff). One possible caveat to consider is that we have already had our recession…the Schwab/Yardeni “rolling recessions.” Different parts of the economy have struggled at different times in the post-Virus Fear years (post the sugar rush from the free money train). This, too, is plausible. But we would think the best-case scenario would then be for middling economic growth.



- ➢ Business surveys for Manufacturing are getting worse

The early look on the S&P Composite PMI has it remaining flat at 50.7 in November vs October. Services improved and Manufacturing dipped (back below the breakeven level).

The Philly Fed Manufacturing Index remains in negative territory although it did improve thanks to a better outlook on capex spending (but it is still negative, too). The Kansas City Fed Manufacturing Index was similar.

The Dallas Fed Manufacturing index for November remains in deeply negative territory.

The Richmond Fed Manufacturing index for November moved back into negative territory.

Historically, these surveys have been very good leading indictors of future economic activity. But they have been dead wrong for a while now.

- ➢ Other data is weakening
  - Weekly Jobless Claims and Continuing Claims both ticked higher two weeks ago. But both of these reversed lower this week (this week's data was pulled forward because of Thanksgiving). Right when a trend higher was developing, it jerks back lower.
  - Durable Goods reversed sharply lower -6.7% (vs +5% in Sept). But the Core Capital Goods Orders, aka business spending, only fell slightly. And this was an improvement (-0.2% in Sept and -0.1% in Oct). Transportation items were the major swing factor.
  - Industrial Production fell -0.6% in October which also follows a lower revision in September. Capacity Utilization fell below 79% for its lowest reading of the year. Manufacturing Production fared worse.
  - 3Q GDP was revised higher from 4.9% to 5.2%. This was primarily driven by higher government spending than previously thought (ugh). (Investment spending was positive, too.)

- Both Retail and Wholesale Inventories fell in October.
- University of Michigan's Consumer Sentiment gage fell for the fourth month in a row.
- Germany's economy shrunk in the Q3 as expected.

➢ OPEC production cuts are likely to outpace Russia sanctions

The US has sanctioned three UAE shippers that have been delivering Russian oil above the $60 price cap. We have long said that the Russians are brazenly ignoring the sanctions…and why wouldn't they if they have complicit shippers and buyers? But it now looks like the US is getting more serious. But slapping shippers one at a time will be a slow bleed. Of course, the US government does not *really* want to see Russian oil disappear.

OPEC+ is struggling to reach a consensus for future production cuts. Saudi Arabia wants to keep the reigns tight, but some of the other members are looking to increase production. Some of the African members are becoming increasingly skeptical of the limiting quota system (Nigeria, Angola, Congo (not the Zaire one)). We think Saudi will win over its brothers in crime/cartel. If not, they probably have the will and the means to keep up the production cuts by themselves (they will exhaust of this over time, but politics with the US are likely playing a large roll).

➢ Where did all the crypto money go?

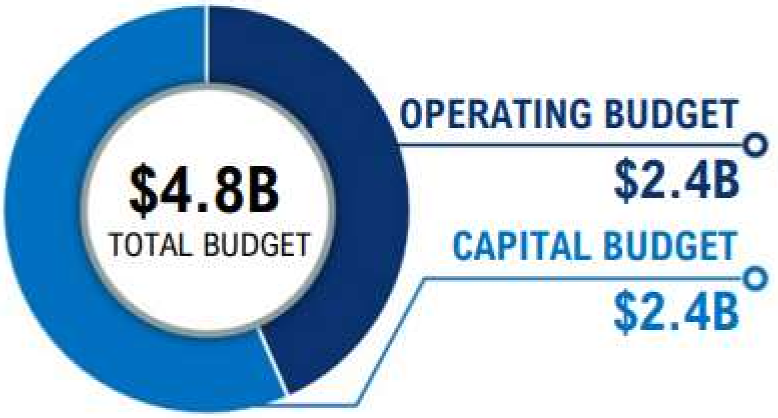
Two executives from FTX are starting a new crypto "exchange" called Backpack. The company and its affiliate will be located in Dubai and the British Virgin Islands. Their tag line is, "In a post-FTX world, you need trust and transparency to create a true alternative to the other players."

It was only a matter of time, but Binance, the world's largest crypto platform (do not call it an exchange!), has fallen victim to the US legal system. CZ, the mysterious founder of Binance, has been ousted and might actually serve some time in jail (a short stint at a country club outpost is most likely, but there are varying reports of potential sentencing). The company must institute some vague anti-money laundering procedures. Considering the DOJ has evidence of a company insider putting in a chat, "We need a banner 'is washing drug money too hard these days? Come to Binance, we got cake for you'." But the real meat is the company has to pay a $4.3b fine. And it can keep operating. Yeah, snort, it's about the money.

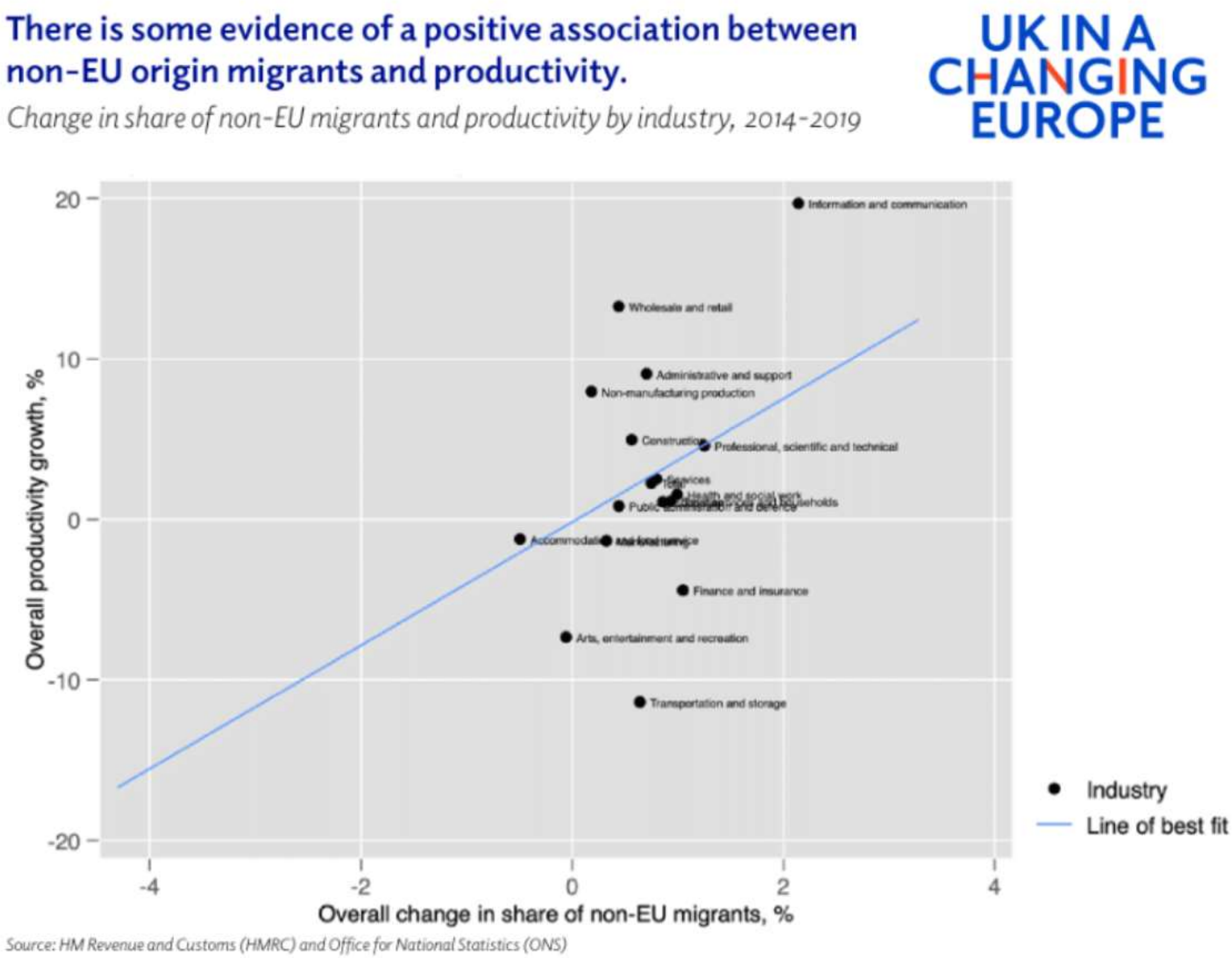
➢ Chart Crime(s) of the week(s)

This is the official budget proposal for the Washington DC Metro system.

METRO | AT



And this is from a professor who likes to argue with people on Twitter about the voracity of his social science data (contradiction?). His argument is that non-EU immigration into the UK increases productivity. A Musk monkey with the Neuralink implant could draw a line that better represents this data.



- Quick Hits
  - A research study in Australia concludes that "taking selfies" poses a "public health problem" because idiots fall off cliffs and do other dumb things (seriously).
  - 60% of MMA fighters sustain injuries. If a loser is injured, it is a concussion 17% of the time. (These numbers seem very low to us.)
  - The Census Bureau wants to spend $10mm to figure how to best ask questions about "gender identity."
  - CNBC reports that the lack of EV charging infrastructure (locations and speed) is an impediment to consumers. Generalissimo Franco…dead.
  - Georgia is the first team to go 8-0 in SEC conference play for three straight years.
  - Crazy Cathie Wood, aka the Woodchipper, reiterated her $1mm price target on Bitcoin.
  - A hacker contacted the SEC to file a whistleblower complaint. The hacker's victim had not disclosed the hack within the four-day window that the SEC suggests (and will soon mandate).
  - New York state's lowest level of state court is called the New York Supreme Court.

- Environmental groups are suing the UK government for its fuzzy accounting of “carbon capture” and reducing “emissions.” The government agency thinks that burning wood creates *negative* emissions.
- The Chiefs – Eagles Monday Night Football game was the most watched TV show of the year. (We find this stat misleading because it excludes specials like the Super Bowl.)
- Until the Cowboys whooped the Redskins on Thanksgiving. That was the third most watched regular season game ever.
- The NFL does not play games on Friday night or Saturdays (in the fall) because of a law passed in 1961.
- The new president of Argentina thinks human organ trading should be legal.
- Thanksgiving Sunday was the busiest air travel day ever in the US. Seven of the 10 busiest days have been this year.
- One of Charlie Munger’s best lines, “Never tell anyone about your problems. 90% of the people do not care. And the other 10% are glad you have them.”

Trading: We increased our long exposure across the board. We added some Energy, Financials, Big Tech, and Healthcare. Our Put options are taking it on the chin. We are going to wait to reload on these. It is hard to fight this kind of momentum. WE are glad we cut some a month ago. But the lesson in this market si to book a profit as quickly as possible on the short side. While our longs are benefiting from this same momentum, we think they are better suited to fend against any economic slowness that may arise. And our large cash position (not as large now) will play the same role as protection (obviously without the leverage, but, again, that short leverage is not your friend in a rallying environment).

TSLAQ: Musk continues to alienate his advertisers on Twitter/X. Apple, Disney, Comcast, Paramount, and a host of other companies have “paused” their advertising after Musk made some flippant comments about the war in Israel (it is worse than this, he made some disparaging comments about Jewish people as a whole). To be fair, the anti-Musk barrage is being heralded by political operatives. But Musk is also an idiot for wading into these waters. Michael Jordan had it right.

As a reminder, the business ramifications are relevant. Musk used expensive debt to help fund the Twitter acquisition. His only source of capital is Tesla stock (and even that might be running low since he has pledged so much to fund SpaceX and his other sillier ventures). And it is no coincidence that he has started to float the talk of taking SpaceX public. That could be a whole new source of capital to keep his shell game going.

There is also news on Musk’s legal front. A judge in Florida ruled that Musk and Tesla knew that the “Autopilot” feature was defective. The widow of a crash victim will be allowed to sue the company for punitive damages for “gross negligence and intentional misconduct.”

There is also burgeoning blowback on Musk’s silly Neuralink. Four congressmen have written a letter to the SEC. They allege that Musk has committed securities fraud during the course of monkey trials. Musk says the monkeys were killed because they were “terminal.” The letter alleges the monkeys died directly from the brain implants. This would hardly be a headline if it were not for it involving Musk. Fair or not, his outspoken behavior is making him a political target which is ultimately bad for business.

Or we could have just summed up Musk’s current state of affairs/mind with his own quote from today. When asked on TV what he thought about Bob Iger pulling Disney’s ads from Twitter, Musk said, “Bob, go F**k yourself” into the camera. He repeated it more loudly just to make sure everyone heard it.

*We have all sorts of stories about government debt auctions. Once, our auction bid for a Mexican Cetes auction was not submitted on time. Our dealer got drunk at lunch and wrecked his motorcycle on the way to the central bank. (Pardon us if we have told this one already.)

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