Weekly Update

25-Mar-2021

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- Is the rotation over?
- China tensions still rising
- Buybacks might start helping the market
- Housing dips, just the weather?
- Durable Goods Orders also slowed in February
- PMI Business Surveys are as strong as ever
- Nasty selloff in oil, probably just profit taking
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
SPX	3910	0.2%	4.4%	62.3%
QQQ	311.3	-0.1%	-0.6%	70.6%
US 10 YR	1.64%	1.65%	0.92%	0.68%
VIX	19.8%	19.2%	22.8%	65.5%
Oil	58.53	-93.0%	20.7%	139.1%

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

The standard rotation has seemingly broken down. That is, Big Tech and higher Growth names have all been under pressure because of the surge in interest rates…the pundits have beaten this theme to death (us included probably). And Energy, Financials, Industrials and Materials were the beneficiaries. But now that the 10 year has settled down around the 1.60-1.65% level, the Growth category is still lagging the market. And the aforementioned Value sectors have stalled out. Utilities and Staples, two common bond proxies, have been performing well. Some point to the Fed hiking rates in 2023 instead of 2024 (now that is some fancy forecasting). Others think Europe's continued vaccine woes will further crimp demand. Along those lines, America's nanny-state brethren (our European-like states led by New York and New Jersey) are contemplating renewed lockdown measures. And despite the "stimmy" money coming down the pipeline, there has been a notable drop in retail participation. There are even some crazy people out there pointing to old-fashioned expensive valuations.

We think rotations typically end this way. The market chops around, decides to split the baby, and sells everything while pointing its finger at all sorts of ephemeral culprits. But without a real catalyst (recession fears, imminent rate hikes, some sort of financial calamity, political/geopolitical upheaval, etc), this selling can often be the point of exhaustion. While we certainly see plenty of room for further stumbles, we also do not think

there is not a crushing catalyst around the corner (plenty in the long-term). We will continue to base most of our positioning off Volatility.

- China tensions still rising

Speaking of negative catalysts, we recently mentioned rising tensions between the US and China, and things seem to be deteriorating more. With China looking to make a government body that essentially takes over all of the data collection from its version of Big Tech (Alibaba, JD.com, Baidu, Tencent, Netease, etc), the Biden administration (or is it the Harris admin yet?) is looking to implement and enforce Trump's Holding Foreign Companies Act which holds Chinese companies to the same standards as American ones (amazing that this took a law). We suspect this will mostly be jawboning and it will not lead to any sustained negative shocks. But we also are not willing to buy any Chinese Tech names just yet.

- Buybacks might start helping the market

Buybacks are on their way back. In 4Q of 2020, 244 of the S&P 500 bought back stock of at least $5mm. This compares to 190 companies in 3Q but still down from 320 in 4Q2019. The total value bought back was $130.5b which is an increase of 28% vs 3Q. But this is still down 28% from 4Q2019. Assuming the Elizabeth Warren wing(nut) of the Dem party does not make Buybacks illegal, this sizeable, natural buyer in the market should be more impactful. (For what it is worth, we do not always agree with companies buying back their stock. But we always agree with companies having the right to buy back their stock.)

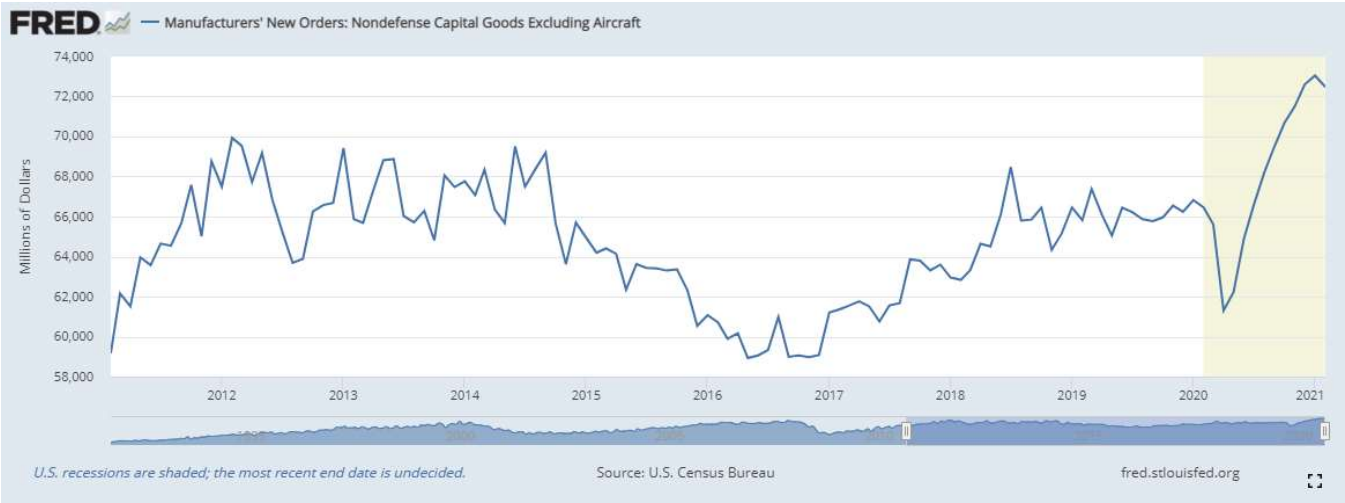
- Housing dips, just the weather?

Housing data took a notable dip in February. Existing Home Sales and New Home Sales followed the poor Housing Starts and Permits reported last week. Existing still grew 9.1% compared to February of 2020. But the annualized pace fell almost 7% compared to January. New Home Sales fell to the lowest level since May of last year. The bad weather certainly impacted the Housing market. But we are a bit confused by the slow down in Existing. This data is based on signed contracts awaiting closing. Typically, bad weather would not be enough to delay a closing (then again, it was one heck of a storm). Nonetheless, the median home price (for Existing) climbed back to its high of $313k. And inventory remains extremely tight at only 2 months of supply. 74% of Existing Homes that sold in February were on the market for less than a month.

Evercore ISI conducted a survey among homebuilders on their view of mortgage rates. Just as we have been espousing, homebuilders do not think demand will be flattened until rates hit about 3.8%. The 30-year mortgage rate currently sits about 3.15%. Of course, as we have noted many times, home builders are the eternal optimists, so a degree of skepticism is worth adding. We still like Housing, but we are cautious about adding and want to see the larger trend continue.

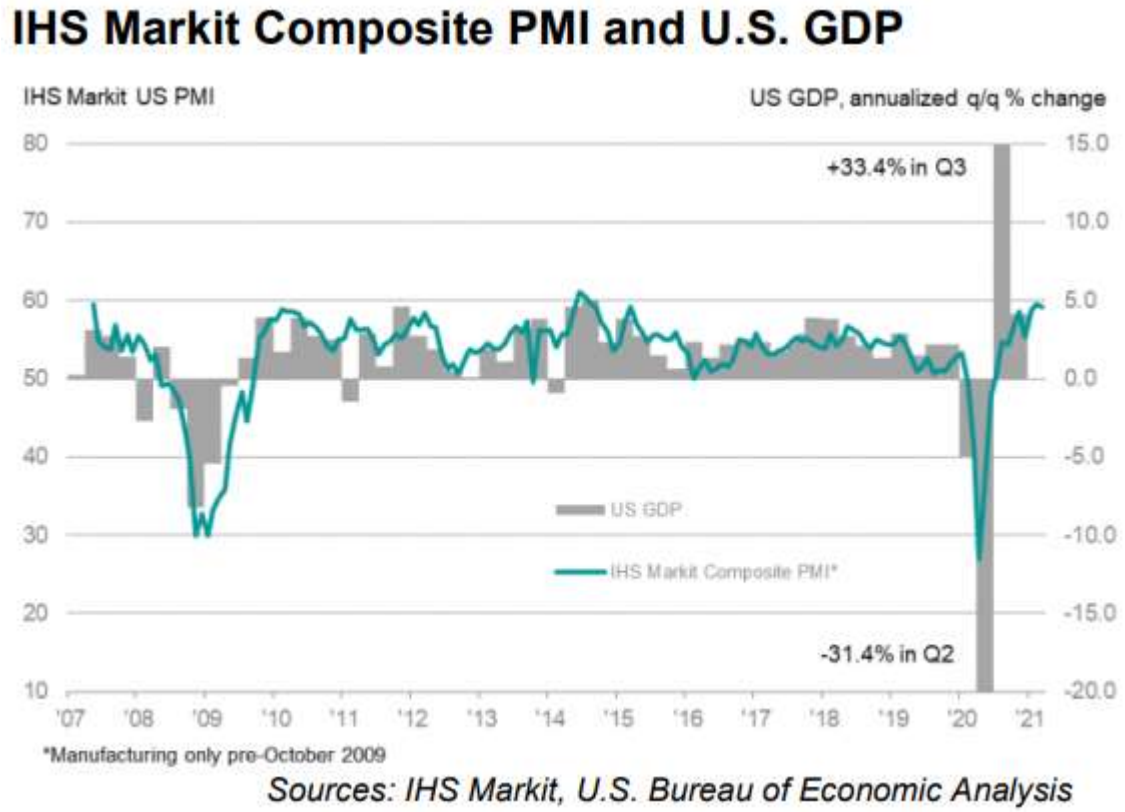
- Durable Goods Orders also slowed in February

Durable Goods shrank in February by 1.1%. This comes on the heels of a strong January increase of 3.5%. The miss was almost entirely in the Core Capital Goods segment…aka busines spending. This is just a minor tick off the all-time high. We will have to see if this is the beginning of a trend (we do not yet think so).



- PMI Business Surveys are as strong as ever

The Flash reading of the Markit PMI showed continued strength across the board in March with a headline reading of 59.1 (sitting just off the high). However, inflation was noted (in the surveys) as increasing on the input side as well as the final selling prices. The Fed calls most of these increases "transitory" because of logistical logjams and what not. Other than ships turning sideways in the Suez Canal, most of these supply chain disruptions seem more secular than one-offs. But with this inflation will come strong GDP. These overlapping data sets look concurrent. But remember, we do not know the GDP performance until after the fact. In other words, the PMI is a true, leading indicator (unlike the official Leading Economic Indicator which is composed of previously released data).



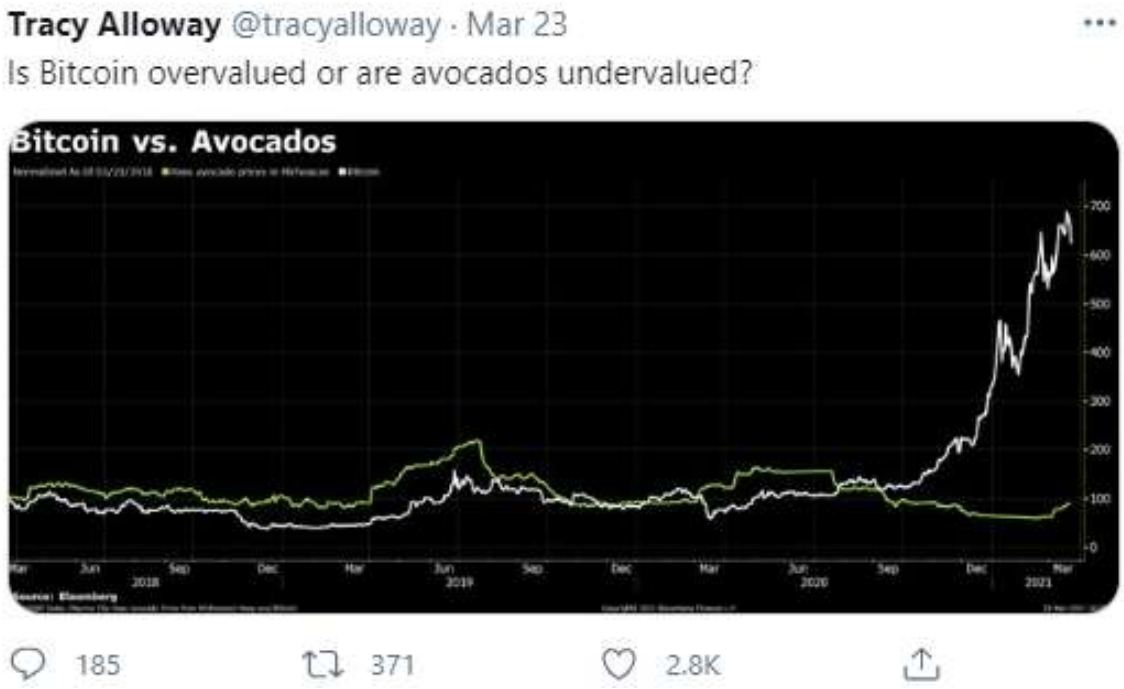
Along with this PMI data came strong regional Fed survey data. The Philly Fed Manufacturing Index surged to its highest level in over 50 years. It more than doubled from 23 in Feb to almost 52 in March. This is one of the largest "beats" in economic data history. The Richmond Fed Manufacturing Index also posted a strong and steady number. The same is true for the KC Fed Manufacturing Index.

- Nasty selloff in oil, probably just profit taking

Crude oil experienced its first nasty sell-off since September. Last Thursday had a 10% drop with the recent drawdown (peak to trough) being about 15%. The finger pointing was fairly predictable. Tensions with Russia are on the rise after Biden called Putin a killer. Russia's only real economic rebuttal is to pump excess oil. European demand might remain weak because of the poor vaccination rollout. And some are pointing to the shape of the oil curve. With near-term prices below those out in time, producers are storing more oil which just reinforces the pricing pressures on near-term futures. And supposedly the Chinese are back to their old tricks and buying more oil from Iran and Venezuela. Of course, a pullback is only logical after the manic run from the negative lows last year in April. We think inflation will continue to be on investors's minds. And long oil is the best way to play this. We would add that Merrill does not agree. They think the "oil plunge (is the) first sign of potential regime shift to higher yields – lower growth." Then again, the same ML research piece thinks we are on pace for "dollar debasement and/or an asset bubble"…just as we have been writing. Quite frankly, we think this is the perfect recipe for oil assuming growth/demand remains on track. There will be plenty of hiccups as there always are (Inventory data, storms, giant ships stuck in a canal, dealing with the whims of the Saudis, Russians, and Chinese…), but we will try and use these to our advantage as long as the great trend is intact.

- Chart Crime of the week

A friend of ours sent us this one from a Bloomberg columnist. Bitcoin vs Avocados? The only question here is, who cares?



- Quick Hits

- Kanye West is worth about $6.5b.
- Junior-level Goldman Sachs employees put together a presentation detailing how much they are overworked and how terrible their lives are. No word on how long it took to put together said PowerPoint.
- Chalk Creek has a no-complaining policy. Instant dismissal and eternal shame are the penalties.
- The White House says $350b of the $1.9t "aid package" is going to help state and local government budgets. The WH did not comment on the federal budget.
- The Turkish President Erdogan (pronounced Er-doe-waun) fired another central banker. This one, the fourth in two years, hiked interest rates. The president thinks hiking interest rates lead to inflation (opposite). And as we like to remind people, he also believes in ESP.
- Evanston, Illinois has approved reparations for blacks who were descendants of someone who lived in the city between 1919 and 1969. They can be eligible for $25k in home repairs.
- Plug Power (PLUG) has issued more stock than it has had revenues in its 22-year history.
- WeWork lost $3.2b in 2020. It is trying to get bought in a SPAC deal.
- Two Democrat Senators vowed to vote against all Biden nominees that are white. They subsequently backed down, but not before claiming that Kamala Harris does not count as Asian because only her mom was Indian. Or perhaps the phrasing is her mom was only Indian. We are not sure.
- Merrill, the king of surveys, has another survey that shows that wealthy, private investors prefer Growth over Value by the largest margin in five years. These same rich people expect Value to outperform. (You read that right.)

Trading: Recently we have been adjusting our exposures between Value and Growth trying to go against the grain. We are balanced at the moment…right when it feels like the standard rotation might be over (as discussed above). Part of this balancing was adjusting our Put option positions. We still have some positions to increase (ones that we think have been under undue pressure). We will likely increase our broad market protection as we increase our Net Exposure. Currently, we have the lowest broad market exposure we have had in more than a few years. While we are still bullish, obviously, we think the days of blindly buying the index (or its leaders) are over for now.

We added a few more names into our Trading model. Sometimes, this bucket houses names that can graduate to a larger, full-time position. Sometimes, they are just short-term plays with a theme or catalyst. We try to keep these balanced so as to not get caught offsides in terms of "factor" exposures. We suspect two of these new names will transition into full time positions while the other two are more trading oriented. Right now, many of our short-termers are Recovery plays. We have some Retailers and Energy stocks in here. But we also have our Housing exposure on watch here. We also have some more hard-catalyst ideas…stocks that will have a restructuring of some sort or a more esoteric theme at heart. Included in our maybe-long-term candidates are a smattering of Old Tech, FinTech, and Auto (not Tesla!).

TSLAQ: The UK has changed its EV subsidy platform. The maximum car price eligible for the GBP$2500 subsidy (reduced from GBP$3000) is now GBP$35,000 down from GBP$50k. We will see if that recent Tesla price hike is going to stick with this double whammy of a price hike (no more subsidies). Otherwise, Tesla is pretty boring now that it is an index name that trades with the Nasdaq.

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