Weekly Update

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- Lots of hype, same Fed path
- Do not bet on the weather
- Positioning: Same old story (everyone is bearish, but everyone has been buying)
- Some Disinflation is here, maybe, but so what
- The Fed repeats the same message: Higher for longer
- FTX: Where has all the money gone (this might be a new category)
- Quick Hits
- Chart Crime of the week
- Trading Update
- Tesla Files (not to be confused with the Twitter Files…although they are similar)
- This guy discovered fusion

	Last	5d %	YTD %	1yr %
S&P 500	3,995	1.6%	-15.2%	-13.1%
QQQ	$286.51	2.1%	-27.6%	-26.5%
US 10 YR	3.48%	3.43%	1.51%	1.46%
USD/DXY	103.6	105.1	96.0	96.5
VIX	21.1%	22.7%	17.2%	19.3%
Oil	$77.42	7.5%	2.8%	9.3%

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

This was a hype-filled week with inflation data followed by the Federal Reserve's interest rate decision. Ultimately, the path of equities did not hinge on these CNBC-pumping headlines. That is, the old school stocks performed well while the most speculative corners of the market suffered. That is not to say Growth stocks performed badly, they marched relatively in line with Value. But stocks related to EVs and crypto were the worst performers. This is our basic playbook. We think the economy will muddle through (mild recession for a while). But the excess speculation driven by free money (and in part the bought-and-paid-for government officials) will continue to come crashing down. Of course, there are many pundits quick to proclaim that "we have reached the point of capitulation." But there are plenty of bankruptcies left to be filed and frauds left to be exposed. This sucking of liquidity will be felt in other more legitimate parts of the economy (for example, real estate). As for people's willingness to believe anything, just look at the bogus "fusion" story (Val Kilmer was more believable in Real Genius), and the "cancer vaccine" without clinical trials. PT Barnum was right.

Looking at the touristy data, the PPI and CPI point to higher Services prices but cooling Goods prices. Logically, the Fed hiked its Fed Funds target rate by the expected 0.50% to bring the range to 4.25%-4.50%. The Fed will keep doing what it needs to do to get inflation back down to 2% (from 6-7% currently). Rate hikes might be smaller and fewer in the medium term, but rate cuts are nowhere in sight. In fact, the Fed's expectation for its "terminal" rate is hitting another cycle high. Not that what the Fed predicts necessarily happens! But the market is telling us the same thing…below average growth is here, and asset prices will act accordingly (sluggish and volatile equities, continued yield curve inversion with lower yields overall, a strong USD, a return to normalcy.) The most telling moment of the week was the head fake rally after the lower CPI number. Investors are slowly wising up - mild disinflation is no cause for celebration when the Fed is intent on sending the economy into a recession!

- Do not bet on the weather

It was a few weeks ago that Bloomberg and others touted the weather trends in Europe as a positive catalyst for the markets. We thought investing based on any weather prediction was pure folly.

European Gas Prices Drop as Warm Weather Contains Heating Demand

- Above normal temperatures are forecast over next two weeks

Of course, winter does happen every year across northern Europe. We are short European Financials (which has been a terrible trade, but we still believe the energy crisis will slow the economy).

Arctic Weather Finally Hits Europe and Will Test Energy Supplies

- Positioning: Same old story (everyone is bearish, but everyone has been buying)

Merrill's Fund Manager Survey, the survey that usually has fund managers telling us what they think other people are doing versus what they themselves are doing, highlights bearishness in growth equities cushioned by a reopening in China. Also juxtaposed to this bearish thinking is the view that peak inflation is behind us, the USD is set to depreciate, and peak rates will be here sooner than previously expected. Most fund managers also think any recent rallies have been driven by short covering.

We find this survey increasingly confusing as everyone seems to be talking out of both sides of their mouths. But one chart derived from this soft data is helpful. Investors say they are expecting Earnings will deteriorate, but official EPS estimates do not reflect this pessimism. We think the view often leads the official data, so we expect negative Earnings revisions (on expectations) to come.

And as we have highlighted recently, Merrill has another data analysis that shows their investors (mutual funds, hedge funds, corporates, retail…the whole gamut) have bought equities for five straight weeks now. Even the "everyone is bearish" Tech saw large inflows. We maintain that everyone is not bearish.

- Some Disinflation is here, maybe, but so what

The Consumer Price Index (CPI) increase for November was cooler than expected. The headline monthly increase was 0.1% compared to 0.4% in October (vs 0.3% expected). The annual rate fell to 7.1% from 7.7% (vs 7.3% expected). The "Core" rate increased 0.2% compared to 0.3% last month (and 0.4% expected). This brings the annual rate down to 6.0% from 6.3%.

But many of the subcomponents in the data are not as rosy. The biggest decrease in prices was seen in Used Cars. We have talked about this one a lot – they were a major contributor to inflation and now they are reversing (one reason why Carvana was such a good short. And also why we still have short exposure to Used Car prices). Obviously, Energy prices have tumbled. We maintain that supply tightness will provide support. But obviously recessionary pressures are exacting their toll. As for the increases, Food, and Services ex-Energy were the largest. The driver in this category is Shelter (it also contains Medical Care, but these prices contracted). It seems to us that the items increasing are far more burdensome than the items cooling. Gasoline is thought to be a major consumption item, but it only accounts for about 4% of the CPI, although to be fair it does have an exaggerated impact on inflation expectations. Our thought on Inflation remains the same. It might be cooling, but different components will keep moving around making it hard to monitor. Moreover, Wages are not showing any signs of cooling, and this is where the Fed is most concerned.

However, Indeed.com has some data that shows wage increases for job-switchers are starting to decelerate. November wages/salaries were up *only* 6.5% vs last year. The peak rate of change was in March. Indeed.com says this data tends to lead overall wage data by "several months." Indeed.com thinks wage growth will moderate back to pre-virus-fear levels by "well into 2024." So, this data sounds encouraging on the headline…until you get to the punchline with respect to the timing ("well into 2024").

The Producer Price Index (PPI, input/wholesale prices) increased 0.3% in November vs October. This compares to the 0.3% monthly increase in October which was actually revised higher from 0.2%. The Core moved higher

by 0.4% vs 0.1% last month which was revised higher from 0.0%. The annualized rates are 7.4% and 6.2%. The main take is that prices for Services are going up. Prices for Goods are doing down (except for Food!).

The Atlanta Fed's Business Inflation Expectations cooled to 3.1% for the next year.

The Consumer Sentiment from the University of Michigan moved higher by a few points. This is the survey that is more closely tied to inflation. It has been bouncing around the last few months…just like inflation. But the overall level is still extremely low…logically inversely correlated with overall high prices.

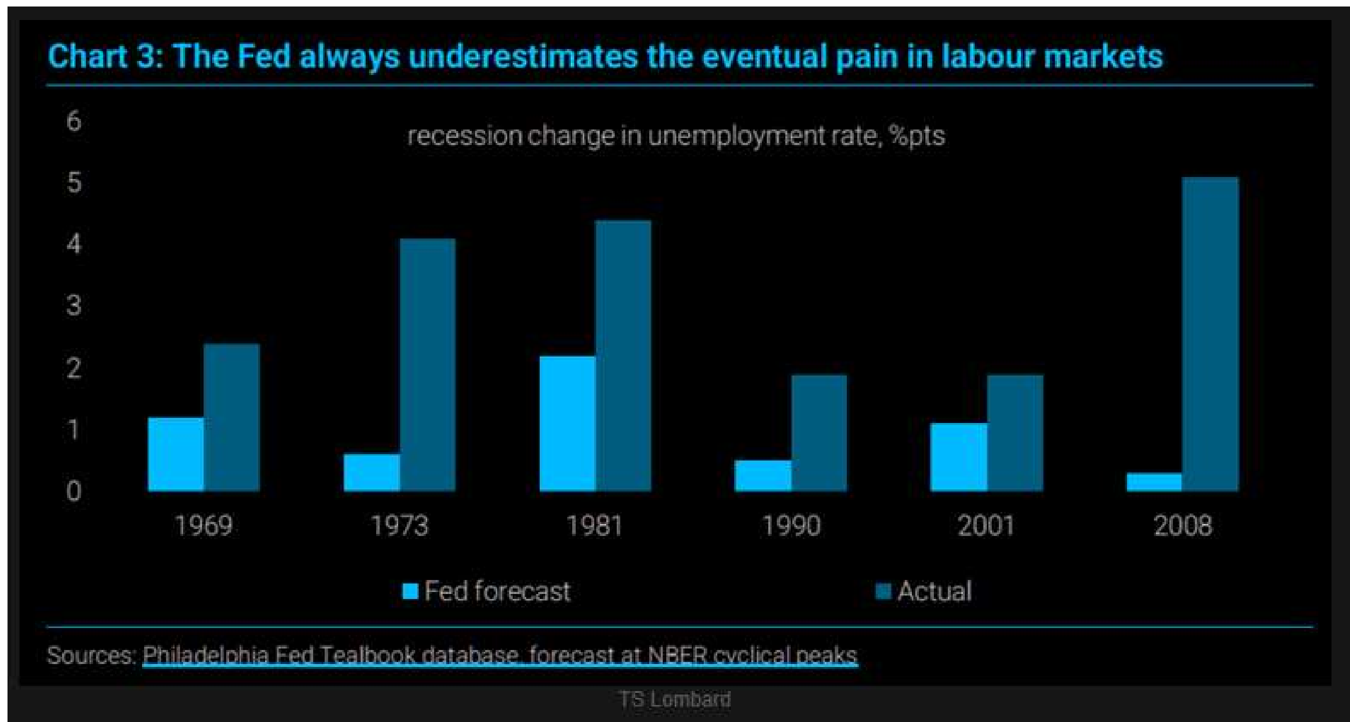
- Other economic data points to further weakness
  - Wholesale Inventories increased by 0.5% in October vs September. This is a mild deceleration which continues the trend from the peak in February earlier this year. But there is still too much inventory for the current demand trends.
  - Small business Optimism (per the NFIB) remained roughly flat near a 10-year low.
  - Mortgage Applications increased this past week. It has been bouncing all over the place recently. But the index of activity is still near a 25-year low.

- The Fed repeats the same message: Higher for longer

Fed chairman Powell has tried to emphasize two themes in all his public addresses. First, he is keenly aware of the mistake the Fed made during the 1970's when it let its foot off the brakes and inflation reaccelerated. And the more targeted message is that accelerating wage growth is the primary focus. Today's press conference after the 0.50% rate hike did not deviate from either of these. Here are the one-liners:

- Focus has to be on getting inflation down
- Seen little progress in wages coming down
- Non-Housing-related Services inflation will take some time to come down.
- The Dot Plot expects rates to get to 5.13%. 17 of 19 FOMC governors and regional Fed presidents think the terminal rate will be at least 5%. Two even believe it will get to 5.63% The expectation in September was 4.6%.
- 25bps in February is on the table
- Firms want to hold onto the workers they have. Doesn't think this Labor market will have a lot of layoffs.
- Inflation decrease will come from Goods and Housing Services
- Policy is getting close to being sufficiently restrictive
- Structural labor shortage in the economy (3.5mm at a minimum). Participation is not moving up. 0.5mm deaths. Early retirements. Immigration has been restricted.
- GDP growth expected to be 0.5% next year.
- Committee won't cut rates until inflation is moving down in a sustained way. There is no view of the neutral rate.
- 2% is still the inflation target and it is unlikely we will change this.

As for the Fed's "softish landing" prediction, here is a good chart (bad graphics) from TS Lombard (via themarketear) that shows just how good, err bad, the Fed has been at predicting its damage to the Labor market.



- FTX: Where has all the money gone?

We have another entry into this new category detailing the idiocy of SBF and his clown-car of crypto fools at FTX/Alameda. They had created some derivatives on make-believe tokens. Theses were often juiced up with leverage of 3x, 4x, even 10x. But like all levered structures, they get out of whack to their mandate, so they must be rebalanced (the same is true for regular ETFs holding regular equities). FTX would disclose the timing and the amount of the rebalancing needed to adjust the structures. This was not printed on billboards or shouted from the mountaintops, but it was publicly available if you looked hard enough. And some clever sleuths did just that. The FTX fools, the ones who claimed to solve the geographic arbitrage of Bitcoin during the early days (and we praised them for this…but now we are doubting it ever happened), got fleeced on their own products.

As for current crypto news, the red flags keep flying. Binance, the world's largest "exchange" (aka shadow bank, hedge fund, broker-dealer, market-maker, payday lender, pawn shop, fantasy land all rolled into one) restricted outflows in one of the larger "stable coins," USDC. The excuse given was that New York banks were not open. And Binance needs a bank to execute the swap (customer sells crypto A to buy crypto B, but crypto A proceeds need to be converted to USDC which then can be used to buy crypto B…easy right?). Other than this proving that there is nothing decentralized about crypto trading (self-custody HODLing is different), the lack of liquidity in these houses of cards should make everyone run for the door.

- Chart Crime of the week

This was presented in a marketing format to tout the merits of a company's trading platform. They even apologized for the fuzziness of it! We would probably *pay* to not use this.

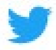
- Quick Hits
  - VinFast, a Vietnamese EV maker, filed for an IPO in the US seeking to raise $100mm. Last year, the company was looking to raise $2b before pulling the plug.
  - The European Commission's foreign aid department spent $400k building a "metaverse" as a promotional tool (to promote the EU?). Five people registered for the first "party."
  - Celine Dion suffers from Stiff Person Syndrome (this is a real autoimmune disorder).
  - Morgan Stanley praised Rivian's joint venture with Mercedes when it was announced three months ago.
  - Morgan Stanley praised Rivian for its capital discipline after backing out of the joint venture with Mercedes which was announced Monday.
  - 25% of millennials (26-41 years old) live with their parents. This is 18mm which is up from 9mm people a year ago.
  - 42% of married couples have a joint bank account.
  - The outgoing governor of Oregon commuted the sentence of every death row inmate because it would bring the families of the victims a "step closer to finality."
  - The UK is opening up a new coal mine for the first time in 30 years. It will be mostly sold to foreigner buyers in the steel market.

Trading: We dipped our tow back into Energy after having trimmed some. We cut some of our long Retail exposure. We believe our holdings to be idiosyncratic to the broad Retail landscape. But after strong earnings and good performance, we took some profits (we also think they might succumb to the post-Christmas malaise we are expecting). We also added to some short exposure in the Fantasies and Frauds. We will likely rotate more short exposure away from plane-Jane recession stocks to the structurally challenged F&F.

TSLAQ: The Bond Villain is trying to convert some of Twitter's debt to margin debt collateralized by Tesla stock. This is the debt that has an 11.75% coupon, and nobody wants it at $0.60 on the dollar. The bank underwriters are holding on to it for now. But they obviously want to get this off their books. Margin debt is not their first choice, but its better than going down with the ship.

Remember those Shanghai production cuts that Tesla denied last week? They announced production cuts in Shanghai. At least the lie cycle is shortening.

Check out our website to learn more about Chalk Creek Partners

 Carlisle's Twitter Financial List

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