Weekly Update

15-September-2021
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- The market treads water…waiting for something
- Companies and Insiders are selling stock
- How might Value win?
- Merrill Fund Manager Survey stays long Growth stocks but not the Economy
- Jobless Claims continue to trend lower
- Don't believe the hype (states don't want the federal money anymore)
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	Last	5d %	YTD %	1yr %
SPX	4481	-0.7%	19.3%	33.7%
QQQ	378.1	-0.7%	20.8%	37.2%
US 10 YR	1.30%	1.34%	0.92%	0.69%
USD/DXY	92.5	92.7	89.9	93.2
VIX	18.2%	18.0%	22.8%	26.0%
Oil	72.63	4.7%	49.7%	89.7%

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

The market continues to tread water as not much has changed with the narratives. There seems to be a consensus that the Fed's Powell will keep the tapering of the bond purchases slow and orderly (as will the ECB). More importantly, interest rates will not be moving any time in the foreseeable future. Gridlock has taken hold of the political landscape. We are waiting to see if the ex-workers on the couch go back to work when/if they notice the missing monthly government checks (more below on the fake narrative that this is not an incentive to work). And, of course, most people are trying to read through the garbled messaging around the virus. We have commented recently that the market shrugs off bad news and keeps dancing to the Fed's beat. But if one of these narratives gets derailed (and not just shook a bit), we could see that long awaited 5-10% pullback. Obviously, it is impossible to call these things much less time them. Nonetheless, our skepticism over market perfection is running high, so we will continue to trim some long exposure.

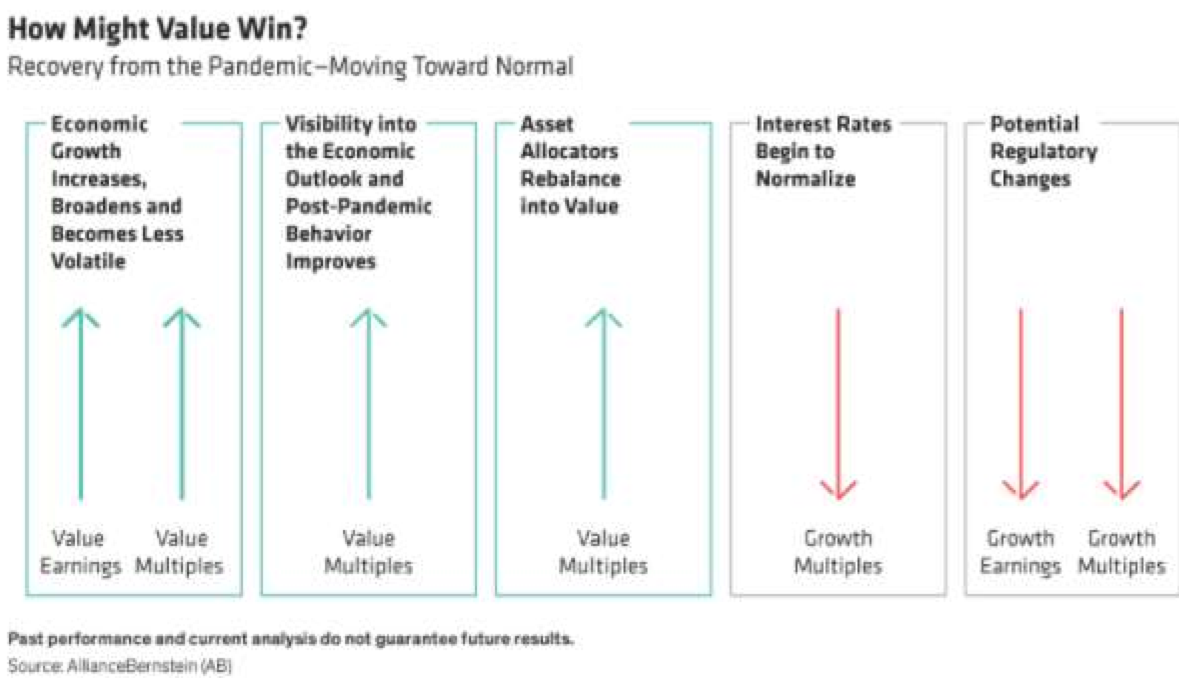
On the political front, the $3.5t "human infrastructure" bill is still stalled. Much of the media is holding out hope pointing to Joe Manchin's (D-WV) comment, "I don't see the urgency" as just a matter of being prudent. When pressed whether it was a timing issue or if the spending amount was too much, he flatly said "oh it is the $3.5t amount." Elsewhere, other moderate Dems have changed their goals for new tax rates with only modest increases (notably the capital gains tax would only go from 20% to 25% and not near 40%, the "stepped up basis" upon death would not be changed, but there would be a surtax for incomes over $5mm). All of this is positive as even the Larry Summers wing of the Democrats realize the spending must slow at some point. But the market has gotten hooked on the short-term fix of free money, so the withdrawal might be painful. Elsewhere, Newsom kept his job in California rather easily. This is probably a non-event (a recall would have been a huge event). And Oil & Gas might be keeping its tax loopholes (more below).

- Companies and Insiders are selling stock

Anecdotally, we are starting to see more block trades. Some are companies raising capital, and others are insiders taking profits. This is historically a good indicator of market direction (unlike buybacks which can be a contrarian indicator after the buying is done…Microsoft's announcement of a new $60b buyback undoubtedly helped the markets today).

- How might Value win?

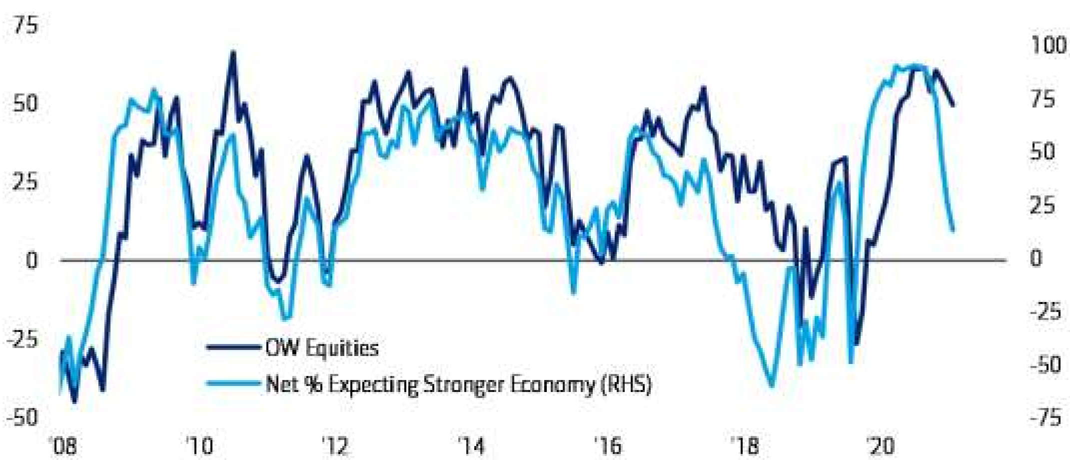
This is a chart from Bernstein research describing how Value investments might "win." We do not think the first block will come true as growth will slow and remain volatile. Visibility into post-pandemic behavior is impossible to predict and will remain that way (Covid Forever). Asset Allocators will only shift to Value if Value is already starting to win (tautological but true…what does this say about asset allocators?). Interest rates will not normalize any time soon. The only one with a reasonable chance of happening is that Regulators will turn up the heat on the market heavy weights (all Growth stocks). We are long some Value for balance and for trading angles. But going through this exercise sure does not make us want to run out and buy more Value.



- Merrill Fund Manager Survey stays long Growth stocks but not the Economy

The latest survey of large institutional fund managers shows that institutional investors are still "overweight" equities with Growth stocks leading the charge. They think the Fed will ease into the tapering and keep interest rates low forever. Investors have given up on the Reopening trade with minimal exposure to small-caps, Value, and Inflation. The percentage thinking there will be a "stronger economy" has plummeted. We mesh with most of this thinking (yikes) except for the possibility of both a recovery (we have some small-cap exposure) and inflation (not our base case, but we have some exposure just in case). We also obviously have some protection, so we would not call ourselves "overweight" equities. Whatever the case, it seems like most investors have gone through the Bernstein exercise and have come to the same conclusions. We hate being in the group-think.

Chart 1: Rare FMS disconnect between asset prices & fundamentals growing
Net % expecting stronger economy vs net % overweight equities



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

- ➢ Jobless Claims continue to trend lower

Jobless claims fell to a virus-fear low of 310k. This is only about 100k from the 2019 average. Of course, these are New claims (we usually reference the Continuing Claims). So, the falling number tells us that employers are holding onto workers as best they can. It does not mean laid off workers are getting off the Family Guy couch at a face pace. Recall the August Employment Report showed positive job growth but far below expectations.

- ➢ Don't believe the hype (states don't want the federal money anymore)

One thing we came across that has not been mentioned in the media: Every single state declined more federal unemployment assistance before the September 6th expiration. For all the belly aching and pseudo-science about how states (all red) that opted out of the federal pandemic unemployment problems showed only small increases in employment, we now know that it was all politics. Even the blue states acknowledge that paying people not to work is not the best thing for sustained economic growth.

- ➢ Is Inflation sticking? Too soon to tell

The Consumer Price Index (CPI, consumer inflation) for August was slightly lower than expected with a monthly increase of 0.3% vs July's 0.5% increase. This is still a 5.3% gain vs August of last year. The "core" increased 4% vs last year.

The Producer Price Index (PPI) for August showed the wholesale price surged about what was expected. 8.3% was the increase vs August of 2020. While the monthly growth (vs July 2021) was robust at 0.7%, this is down from the 1% growth in July vs June. The "core" reading (excluding food and energy) showed similar, relative increases: 6.7% annual and 0.6% monthly. As we have been writing, this is a bad recipe for corporate margins if it continues. This explicitly tells that either companies do not think their input prices will remain elevated, or companies do not think there is enough demand for their products at the higher prices (that would reflect all the wholesale price increases).

As for inflation expectations, New Yorkers (and surrounding areas) are fretting more than southerners. The NY Fed's Survey of Consumer Expectations has an inflation component: the median expectation for inflation over the next year is 5.2%. The three-year expectation is better at 4%. On the other hand, the Atlanta Fed's Business Inflation Expectation reads 3.1% (one year outlook). Other than psychological differences (people in the NY area tend to fret more than your average American…this is our experience not some scientific analysis), we think the infrastructure is more strained in the NY area and thus more susceptible to problems with logistics. Our unsupported assumptions aside, we still think inflation will cool. So, in the meantime, we still have some long-inflation exposures (energy and financials). But we also think this inflation does ultimately subside at the same time the economy starts to cool (people stop paying the higher prices and thus spending falls). We do not want to be in these sectors when that happens.

Here is the latest shipping container backlog in US ports:

- The ECB joins the Fed in its own (wimpy) way

The European Central Bank has decided to slow down its bond purchases because of the strength in the economy. The ECB uses similarly vague verbiage as the Fed: it will buy bonds "at a moderately lower pace." The March message was, "at a significantly higher pace." Alas, the ECB will be buying the same amount of bonds. Nonetheless, the market reacted to this relative tightening of monetary policy by pushing yields lower further into negative territory (opposite of what should have happened). The market has since normalized a bit (rates slightly higher but still absurdly negative). The point: We think this will embolden the Fed to slow its asset purchases.

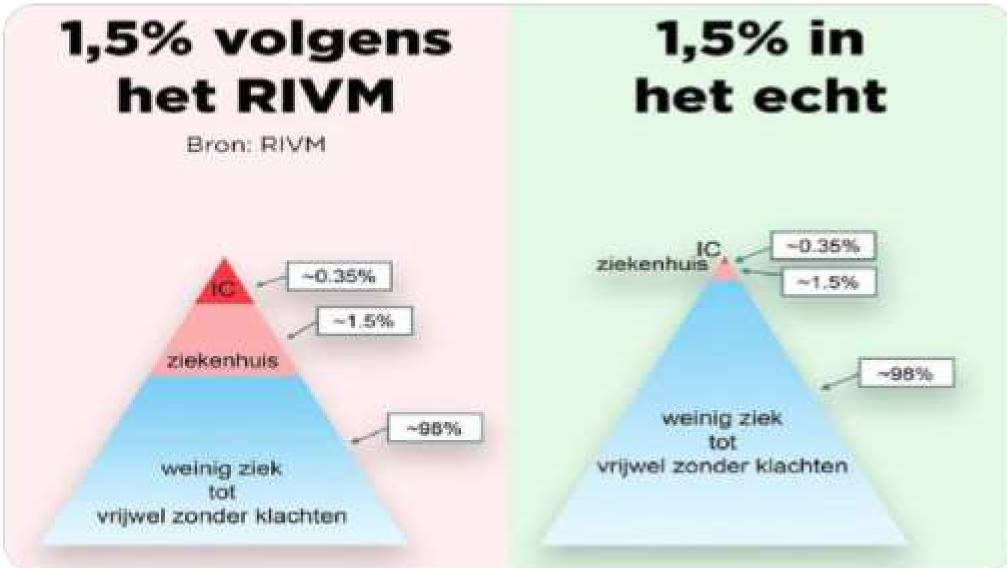
➢ The Chinese cannot keep a good oil down (and the Dems really do not want to)

China wants to continue putting its finger on the scales of commodity prices globally. It has already tried to lower the price of copper, aluminum, and zinc by selling reserves. Now the Chinese claim they are doing it with oil. These attempts are usually short lived if not outright futile. Currently, this modest amount of excess supply is being overshadowed by the slumping inventories in the US (some Gulf refining is still down). There have only been three weeks with positive builds in inventories since March. And oil demand remains steady if not growing on a relative basis. Google mobility trends show "Time Spent at Home" has dropped to about a 5% increase vs 2019 (20% was the peak at the onset of the virus-fear). And the July Total Vehicle Miles Traveled is about 3.5% below the amount traveled in July of 2019 (the downward spikes ex-march 2020 are seasonal dips in the winters).

With the usual twist of political irony, the House Dems have decided to keep the tax breaks for the Oil Industry. Basically, the oil industry is allowed to immediately expense "intangible" costs instead of having to defer them over the life of the revenue-generating period associated with those costs (actually, oil companies can do this for 70% of the costs, the rest is spread out over five years, and it can only be done for US based drilling). These "intangible" costs can account for almost 80% of the total cost of a new well. The Senate Dems will push back against this, but given the tight voting lines, it might be a dead issue (so the loopholes will remain).

➢ Chart Crime of the week

We have learned that most pyramid charts are crimes (not just pyramid schemes). Thus, we were immediately attracted to this one. We had to sharpen our Dutch language skills. The left chart is from the National Institute for Public Health in the Netherlands (RIVM). It is attempting to show the breakdown of the severity of virus cases. IC is intensive care. Ziekenhuis is hospitalized. Weinig Ziek etc is barely sick or no complaints. The right chart is a proper representation of these percentages. It is not just the Germans!



- Quick Hits
  - The former head of ESG investing at Blackrock (Environmental, Social, and Governance) says ESG is a "dangerous placebo."
  - Seat license sales for the Los Angeles Rams have surpassed $600mm.
  - The Denver Broncos reportedly will be going up for sale with a price tag around $4b. The team was bought for $74mm in 1984.
  - Aluminum prices are at a 13 year high.
  - Bitcoin had a *brief* 5% spike higher after a press release from Walmart declared the company would except the crypto Litecoin. It was a fake press release (someone marginally wise once said to watch out for the pumps and dumps).
  - Proposed legislation in the US: EVs (electric vehicles) made in the US by unionized workers will receive about a $12,500 credit. EVs made by mere mortals will only receive $8,000 in credits.
  - Truck drivers under the age of 21 cannot cross state lines (and not just those delivering Coors beer).
  - The current Department of Energy thinks the US can source 44% of all its energy from solar by 2050. The current sourcing level is 3%.
  - The Big 4 accounting firms only make about 36% of their revenues from auditing.
  - Six companies control 70% of the global shipping container market.
  - UK office occupancy rates jumped from 58% to 90% over the last week.
  - Federal tax collection would fall by $91b if the cap on State and Local Taxes (SALT) were eliminated. 52.5% of this tax decrease would go to four states: California (25.1%), New York (16.8%), New Jersey (6.4%) and Illinois (4.2%).

Trading: Activity remains light. We trimmed our net long exposure a bit more. We trimmed some of our Energy and Financial longs (we still like them as an inflation hedge, but worth trimming). We added to our Quality Staples and Retail longs. We are inching into more short positions (via Puts), as well. Most of these are against the highly speculative stuff. Timing these are hard (and time is always against you when you are buying options). We will pick spots slowly. We like to find a balance between trimming longs (tax consequences) and short-term option plays.

TSLAQ: Amazon had this to say about Musk and his SpaceX venture: “Whether it is launching satellites with unlicensed antennas, launching rockets without approval, building an unapproved launch tower, or re-opening a factory in violation of a shelter-in-place order, the conduct of SpaceX and other Musk-led companies makes their view plain: rules are for other people, and those who insist upon or even simply request compliance are deserving of derision and ad hominem attacks. If the FCC regulated hypocrisy, SpaceX would be keeping the commission very busy.”

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