CHALK CREEK PARTNERS

Weekly Update

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Carlisle C. Wysong, CFA
Managing Partner

- Volatile rotations under the surface are likely forced unwinding
- Quality should still thrive despite the economic headwinds
- Credit Card interest is more troubling than the balances
- Leverage Loan maturities are looming
- Inflation is cooling
- Business surveys are split, but none are great
- Labor indicators continue to slowly weaken
- Nobody believes OPEC+, the US government, or US oil companies
- Quick Hits
- Where did all the crypto money go?
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
S&P 500	4,550	0.1%	19.8%	15.6%
QQQ	$385.02	-1.2%	45.2%	34.8%
US 10 YR	4.12%	4.25%	3.75%	3.43%
USD/DXY	104.2	102.8	104.5	105.1
VIX	13.0%	13.0%	22.9%	22.7%
Oil	$69.18	-11.2%	-13.6%	-6.6%

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

The equity market is experiencing some rotation among the sectors despite the flat headline. The pundits are pondering what to make of the recent move out of FATMAAN stocks and into the other 490+ S&P 500 stocks (or into small caps). We think this is primarily trading noise. As in, we are hearing there have been numerous hedge fund blow-ups particularly in the "pod shops" (the gigantic platforms that can have hundreds of teams that work on their own portfolios). This makes sense given the biggest winners in the market have been losers recently. And the heavily shorted Fantasies & Frauds (etc) have all rallied like crazy. A small reprieve in interest rates does not bail out a tanking business. That said, a pullback in the winners is only normal.

The narrative explanation for this trading volatility (despite the headline index, VIX, exhibiting very little volatility) is the move lower in interest rates. Fed chairman Powell did his best to talk down the soft/no-landing euphoria in the market. Or rather, he wants to bridge the gap seen between the bond/oil market (signaling recession) and the equity market (signaling no-landing). "It would be premature to conclude that we have achieved a sufficiently restrictive stance or to speculate on when policy might ease." But more soft economic data reinforced the rate-cutting hopes.

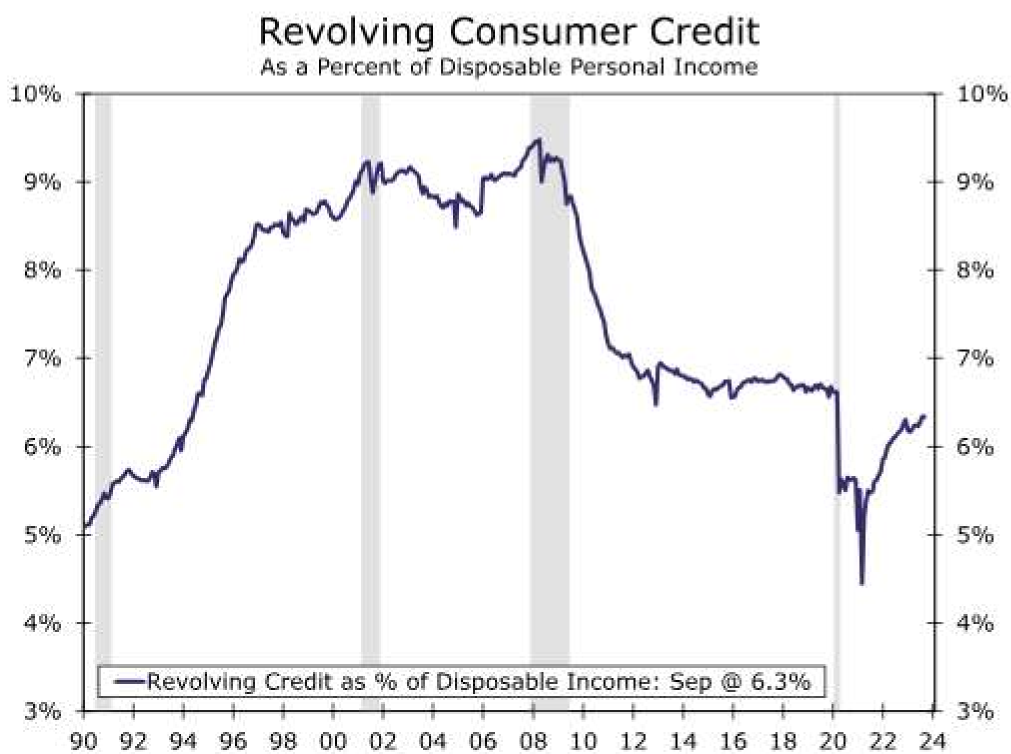
David Zervos (one of the better economists /strategists) points out that the path of disinflation almost perfectly matches what the Fed had in mind according to their "dot plots" (individual Fed member forecasts) last September. And that same dot plot had a Fed Funds target rate of 5.25%...today's rate. In other words, when the Fed predicted that inflation would cool off, they did not expect any accompanying rate cuts. Logically, the only thing that could be different enough to elicit rate cuts now would be a dramatically slowing economy.

Nonetheless, we do think it is possible if not likely for the economy and the market to "muddle through." We expect the large, Quality companies with growth and pricing power and no funding needs to thrive. The more economically sensitive companies with funding needs could suffer.

- Credit Card interest is more troubling than the balances

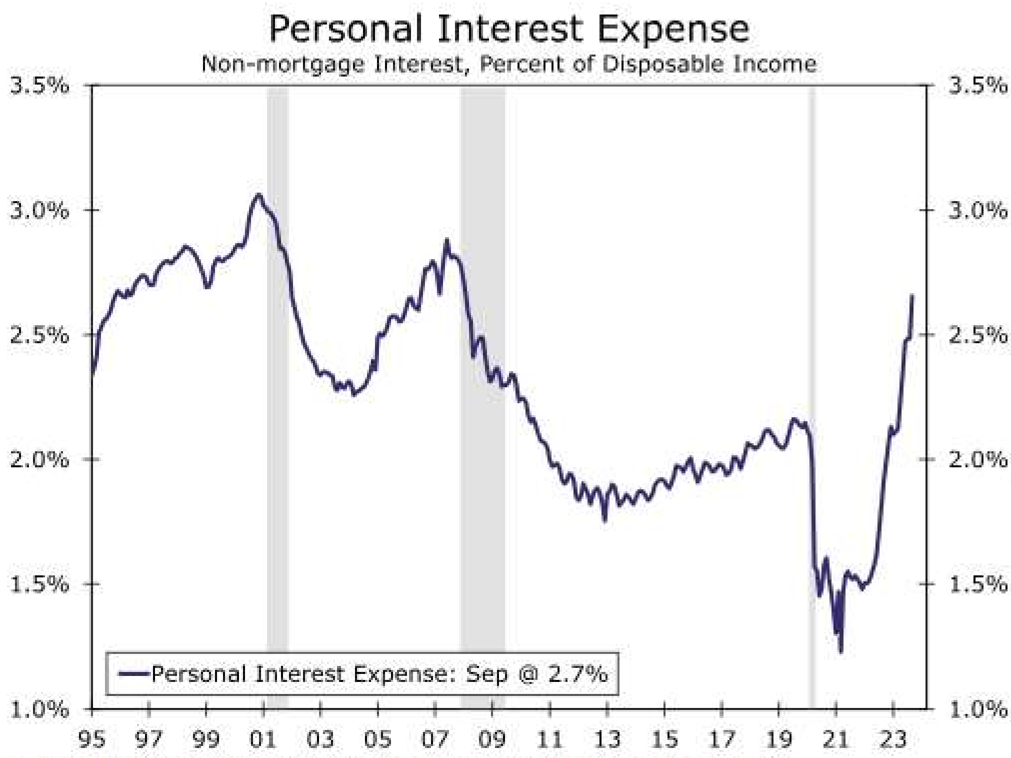
Wells Fargo points out an important distinction between credit card balances, their growth, and interest payments. During the 2008-2020 recovery, credit card balances increased by $80b in total. From 2021 until today, balances have grown over $300b. If you adjust the starting point of the data to the peak right *before* the Virus Fear collapse, this still shows an increase of almost $200b.

However, the level of credit card debt as a percentage of Disposable Income is still low by historical standards. The same goes for total Household Debt to Disposable Income. But considering much of the growth in credit card balances is being shifted away from bank loans (banks have been tightening their lending standards all year), this kind of growth is probably not a good thing (not to mention the use of credit on things like groceries is alarming).



Source: Federal Reserve Board, U.S. Department of Commerce and Wells Fargo Economics

But it is the interest payments that are starting to bite. The non-mortgage interest as a percentage of Disposable Income is rising rapidly. Obviously, the data set is small, but recessions tend to follow sharp increases in this ratio.

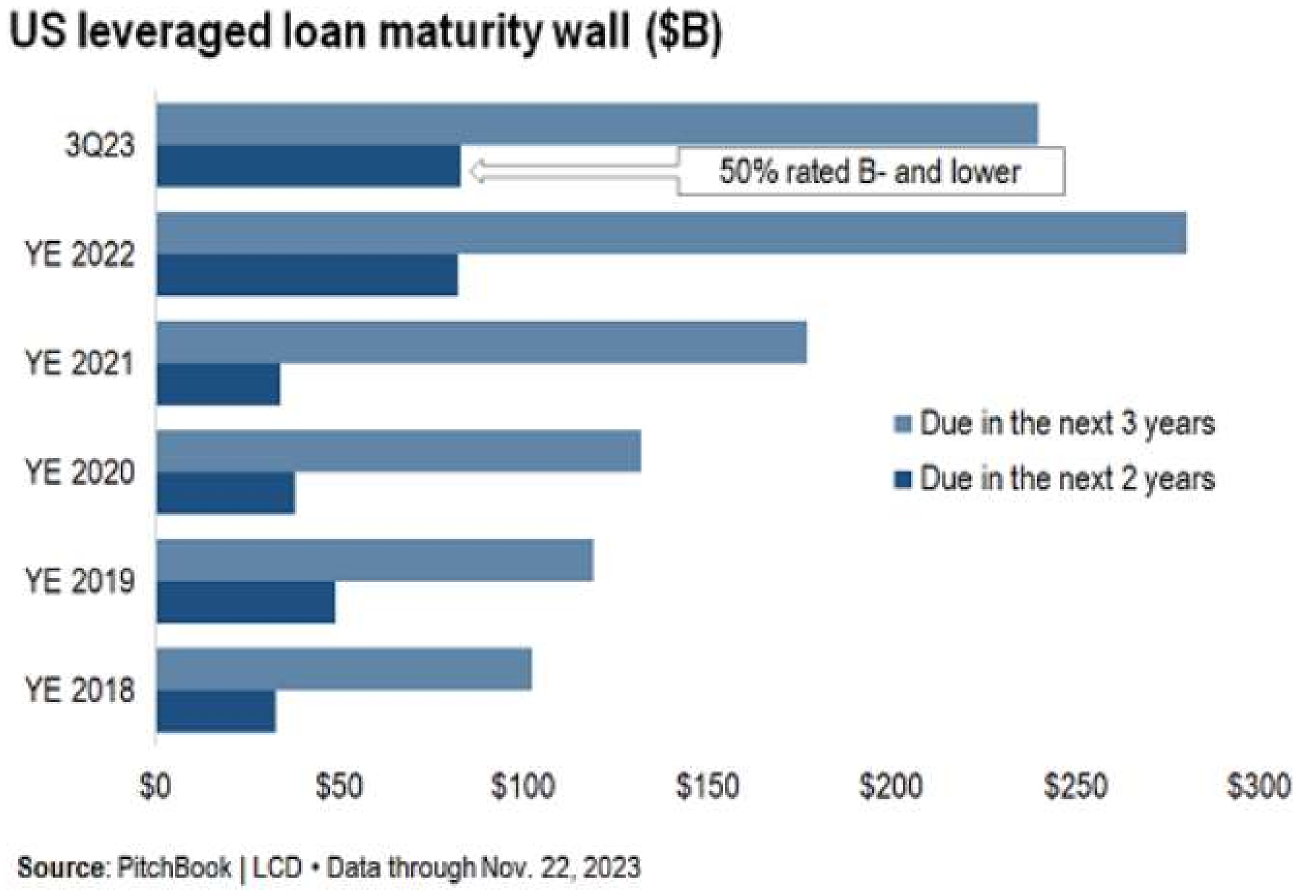


Source: U.S. Department of Commerce and Wells Fargo Economics

Lower interest rates will help. But credit card companies usually are not too quick to lower their rates (but they sure are quick to raise them).

- Leverage Loan maturities are looming

Recently, we have shown some data detailing how smaller companies have a more difficult debt profile: Higher rates and shorter current maturities. The same is true for the riskiest of debt: Leverage loans (junk bonds on steroids). Pitchbook shows that the gross amount of these collateralized loans has more than doubled in the last four to five years. And they note that of the debt due in the next two years, 50% of this is B- and lower. This is solidly in junk territory (C and D are worse, obviously, but B- is a long way from BB+, the highest junk rating).



- Inflation is cooling

Inflation as measured by growth in the Personal Consumption Expenditure index (PCE) cooled from September's increase. The Core slowed from 0.3% to 0.2% which gives us a 3.5% annual increase (down from 3.7%). The downside is Personal Income is also decelerating (0.2% from 0.4% in Sept).

- Business surveys are split, but none are great

Both the ISM Services and S&P Services PMI in November improved slightly (51.8 to 52.7 and 50.6 to 50.8). The better numbers in the ISM reflect a better global macro environment. We think this is reasonable as parts of Europe and Asia have shown signs of life (that is not to say they are doing well…just better).

The Manufacturing PMIs are not improving. But the ISM New Orders component might be rebounding. It is volatile month to month. But the broad trend is improving (still below the breakeven line). The Prices component also strengthened. Even with inflation still being the #1 bogedey man, an increase in Manufacturing prices is probably a good thing (or less deflation as it were).

- Labor indicators continue to slowly weaken

The jobs data ahead of this Friday's Employment Report are signaling more weakness. The JOLTS has Job Openings dropping from 9.55mm to 8.73mm (and that 9.55mm was revised lower to 9.35mm). The peak was in March of 20222 at over 12mm. Quits are subdued…the rate and total number are back down to pre-Virus Fear levels (high Quits are a sign of strength in the Labor market). Some think this Quits rate is leveling off which is a bullish sign for Employment (we think it is too early to declare this). But one strange twist is that America's smallest employers (one to nine employees) account for about 21% of all Job Openings. This is up from the 10-15% range for the last 20 years. We have long claimed that many of the Job Openings are fake news (stale, duplicates, diversity head-fakes*, etc). But we would think that the mom & pops are more accurate in their job listings.

And the number of private jobs added according to ADP fell short of expectations. 103k jobs were added compared to the 130k expected. October was revised lower from 113k to 106k.

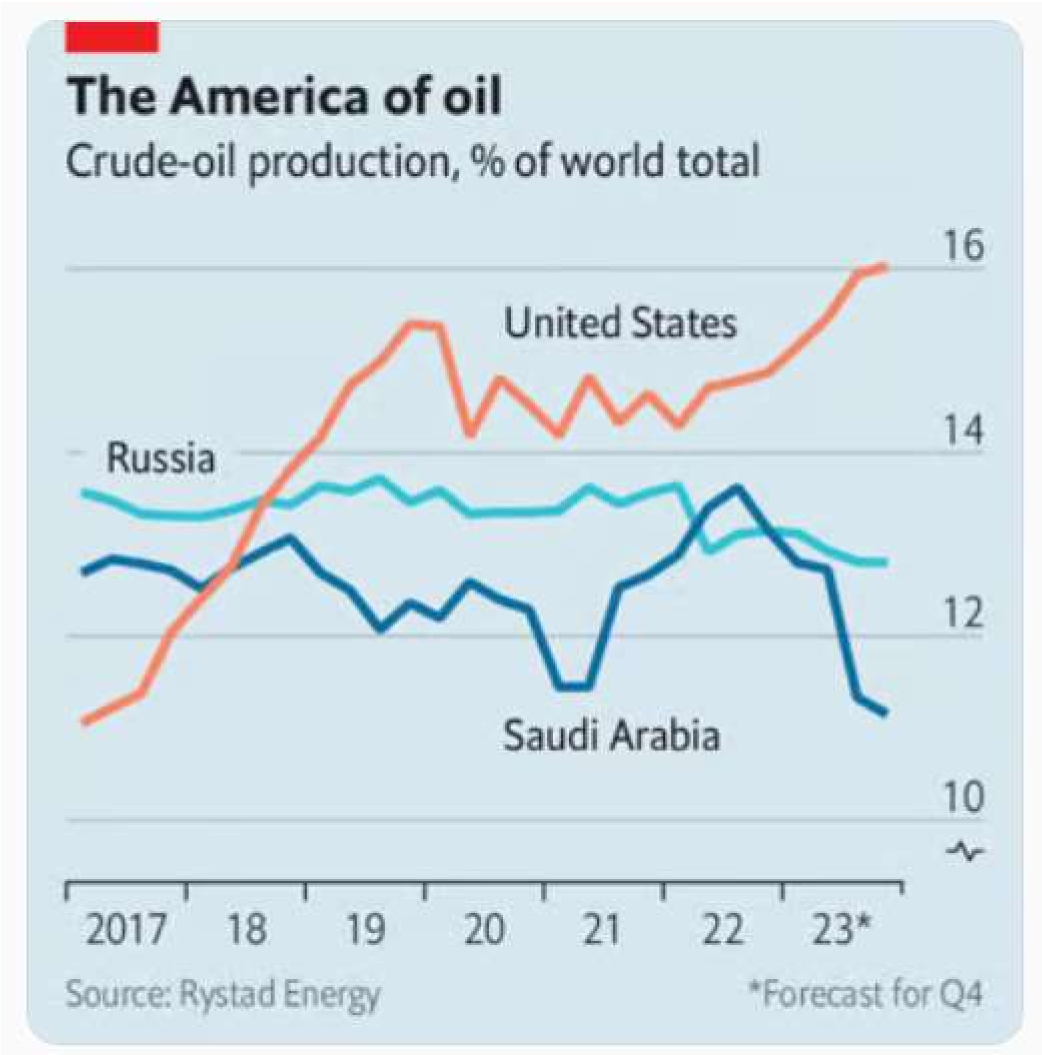
- Other economic data
  - Factory Orders for October flipped to a negative reading (including ex-Transportation).
  - Pending Home Sales fell -1.5% in Oct vs the 1% gain in Sept.
  - Mortgage Applications increased for the fifth straight week. Obviously lower rates are having their effect. This is still just a blip on the medium-term chart, but it is a start.
  - Redbook Retail sales slowed to a 3% gain down from 6.3% during Black Friday week.
  - Nonfarm Productivity in Q3 increased strongly from 3.6% in Q2 to 5.2%. This is a byproduct of stronger GDP output (productivity = output / hours worked).
  - Unit Labor Costs in Q3 also dropped more than expected.
  - The Atlanta Fed's GDPNow for Q4 is 1.3%.

- Nobody believes OPEC+, the US government, or US oil companies

OPEC+ concluded its delayed meeting with a whimper. The group issued a vague statement without a press conference. Saudi wanted the market to know it was extending its voluntary 1mm bpd production cuts (on top of the mandated cuts) into next year as planned. But it appears that many other countries also have voluntary cuts? Enforcement, always an issue, might now drop to zero.

The weekly US inventory data showed a surprising decline. But this was more than ignored by the market. Momentum traders increased their bets on the short side. Why? Because the DOE's "adjustment factor" on some recent data was the largest on record. That is right…the government is fudging even more data.

This is a chart making the rounds. The bears say it shows that Saudi cannot conceivably keep production this low. And despite all the jawboning from the US government- and even from the production companies themselves, domestic production is at an all-time high. Thus, it is likely to stay there. But the bulls say Saudi knows that the US market is full of strong players. It is not like the 2015-6 price wars which were able to crush the bad balance sheets of the myriad small players in the US oil & gas market.

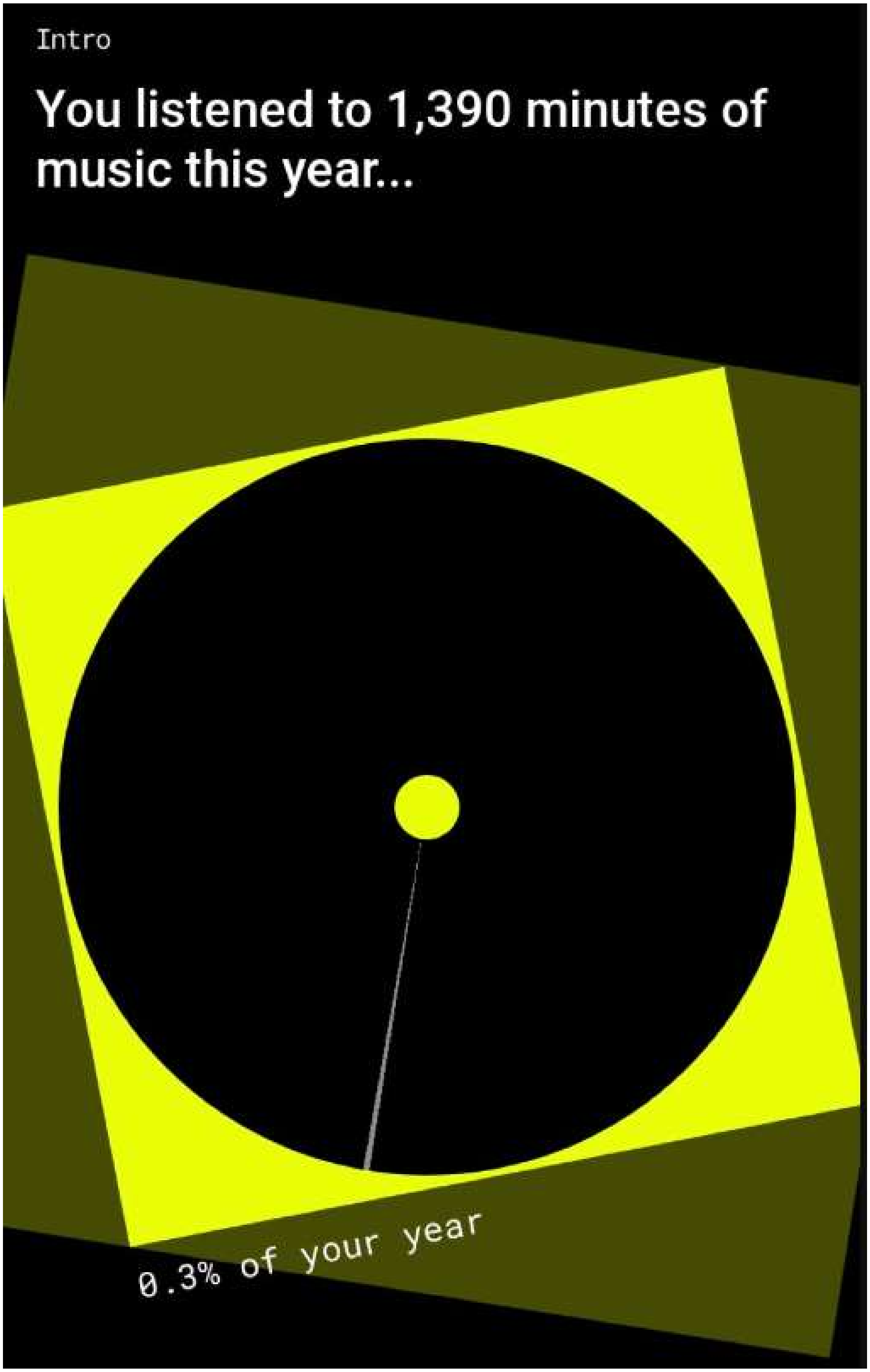


- Where did all the crypto money go?

Crypto bros really do think there is a sucker born every minute. Fifteen minutes after the death of legendary investor and longtime crypto critic Charlie Munger (some of his better descriptions of crypto include, "noxious poison," "partly fraud and partly delusion," "massively stupid," and "disgusting, detestable"), a MUNGER crypto "token" was "minted." It proceeded to rally 31,000% on volume of about $3.5mm. Once these idiots bothered to read the "token's" smart contract (specifically, that creators could restrict the sale…just like the Safe Moon token whose creators are now in jail), it fell 98%.

- Chart Crime of the week

There might not be a literal chart crime here. But the relevance has to be zero. But we are probably in the minority of people trolling the internet who would get the what the pie chart artistically represents.


Intro
You listened to 1,390 minutes of music this year...
0.3% of your year

- Quick Hits

- Iowa's state lottery mistakenly announced the wrong winning numbers. If you were quick enough to collect on your winning ticket during the seven hours until the numbers were corrected, you got to keep your bounty.
- The CEO of Broadcom paid $40k to sit with Xi Jinping at that San Francisco dinner.
- American Airlines is reducing its "carbon footprint" by paying to have sawdust and tree bark compressed and buried.
- Academy Sports and Outdoors was born out of six Army-Navy Surplus stores back in 1938.
- We recently mentioned a fake press release on WeWork for a classic pump & dump attempt. But the press release was not published until after the close on a Friday. And then the company declared bankruptcy over the weekend. The plan was up in smoke. Matt Levine of Bloomberg reports that the fake press release was not published in time because it was formatted incorrectly. If you are gonna be a criminal, don't be a moron (or just don't be a criminal).
- The Cowboys and Seahawks played the fifth NFL game without a punt.
- Scorigami! We missed last week's Denver 29 – Cleveland 12 final score. This is the 1081st unique score in NFL history.
- Scorigami! The Dolphins scalping the Skins 45-15 is the 1082nd unique final score in NFL history.
- The UAE, the host of the latest global warming summit, is the 7th largest oil producer in the world. About 33% of its government revenues come from the oil industry. Yeah, snort, it's about the money.
- The NYT has a bi-weekly segment entitled "Living Small." Last week it featured a $7.2mm, 6,000 sq ft house on Cape Cod.
- GameStop can now invest in other public equities. The CEO can invest in the same stocks as the company. This same CEO pumped and dumped Bed Bath & Beyond before it went bankrupt.
- "Ghost apples" are ice shells that have formed around an apple on a tree. If the apple rots, it falls out the bottom leaving just a shell of ice in the shape of an apple.
- The IRS assessed $1.8b in penalties for underpayment of estimated taxes in 2022.
- Charlie Munger graduated from Harvard Law. He did not have an undergraduate degree.
- Total and Kazakhstan plan on building a $1.4b wind farm which will supply electricity for over 1mm people. (We'll take the over and the under, respectively.)

Trading: We added to our Big Tech longs as they pulled back in this mini-rotation. We also added to some Health Care, Japan, and a couple of more speculative positions (we think after some more work, these might turn into longer term plays, but we think there are enough short-term tailwinds to start positions now). We do not have many short positions on given the manic short squeeze. But we started to add some slowly.

TSLAQ: The media fawned over Tesla's CyberTruck unveiling. Musk blathered on about this being his best product" and what "the future will look like." He proceeded to talk about its toughness. If you recall, four years ago when the first prototype was rolled out onto the stage, his lacky threw a steel ball through the window. Oops. This time around, the same guy soft tossed a baseball with less athletic throwing ability than Lamar (without the javelin aerodynamics).

The point is that this model is completely irrelevant for Tesla. The Morgan Stanley analyst, who is a giant fanboy and beholden to the company since his own company is on the hook for most of Musk's margin loans and Twitter debt, thinks the truck will account for 0% of the company's profits in 2025. (0.0 is better than all courses… incomplete, maybe?)

As for current sales, Tesla's Chinese sales dropped almost 18% in November vs last year. Its market share in China, by far the biggest EV market in the world, has fallen to 5.8% in October down from 8.7% in September.

*Long before the misguided onslaught of Diversity, Equity, and Inclusion policies struck like the plague, financial companies in England were forced to advertise job openings to the masses. While almost every job opening was filled with a word-of-mouth candidate, the companies had to go through the motion of putting the job listing in a public medium. Home & Garden or any other equally useless magazine (in terms of attracting banking talent) were often the home to such fruitless solicitations.

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