Weekly Update

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	Last	5d %	YTD %	1yr %
S&P 500	5,147	-2.0%	8.9%	30.7%
QQQ	$435.26	-2.0%	6.4%	36.9%
US 10 YR	4.31%	4.21%	3.88%	3.31%
USD/DXY	104.2	104.6	101.3	101.9
VIX	16.4%	13.0%	12.5%	19.1%
Oil	$86.74	4.3%	20.9%	7.3%

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

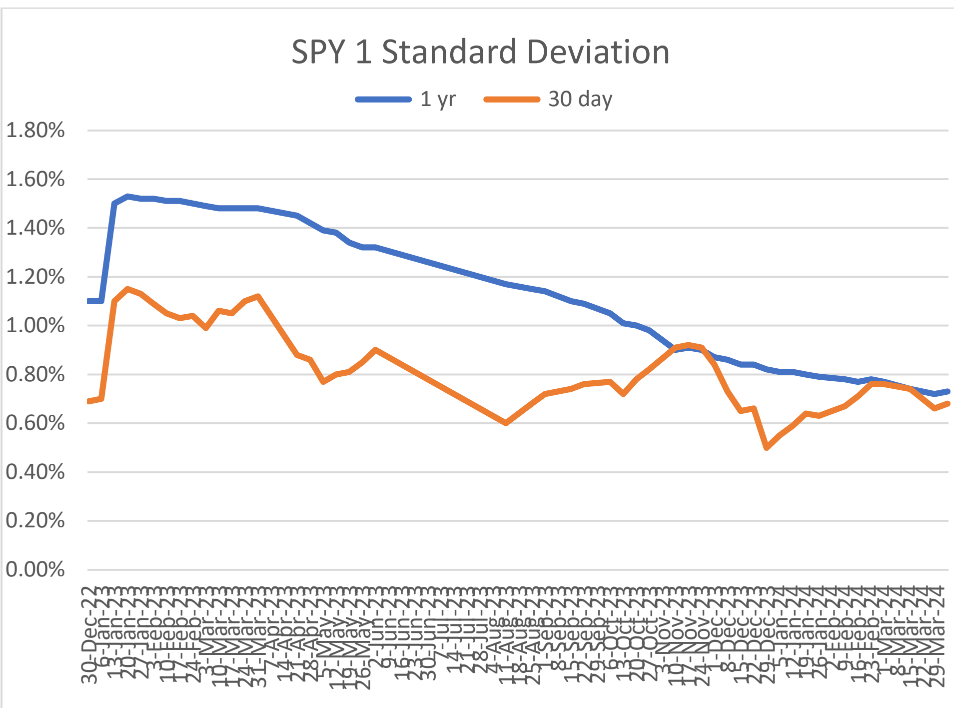
We have been commenting on the choppiness of the market recently. That Volatility took another leg higher this week as strong economic data, crisscrossing Fed-speak, and geopolitical tensions all rattled the nerves of the equity market. A strong Manufacturing survey (of all things) and ADP's preview of the Employment Report gave pause to equity investors…perhaps the economy was too hot for rate cuts (we maintain that the economy does not need rate cuts, but any will be a bonus). And despite an onslaught of Fed voices in favor of rate cuts this year, including Fed Chairman Powell, one outlier voice said, "If we continue to see inflation moving sideways, then that would make me question whether we needed to do those rate cuts at all." By "those rate cuts," Minneapolis Fed president Neel Kashkari means the two rate cuts that he expects the Fed to make!

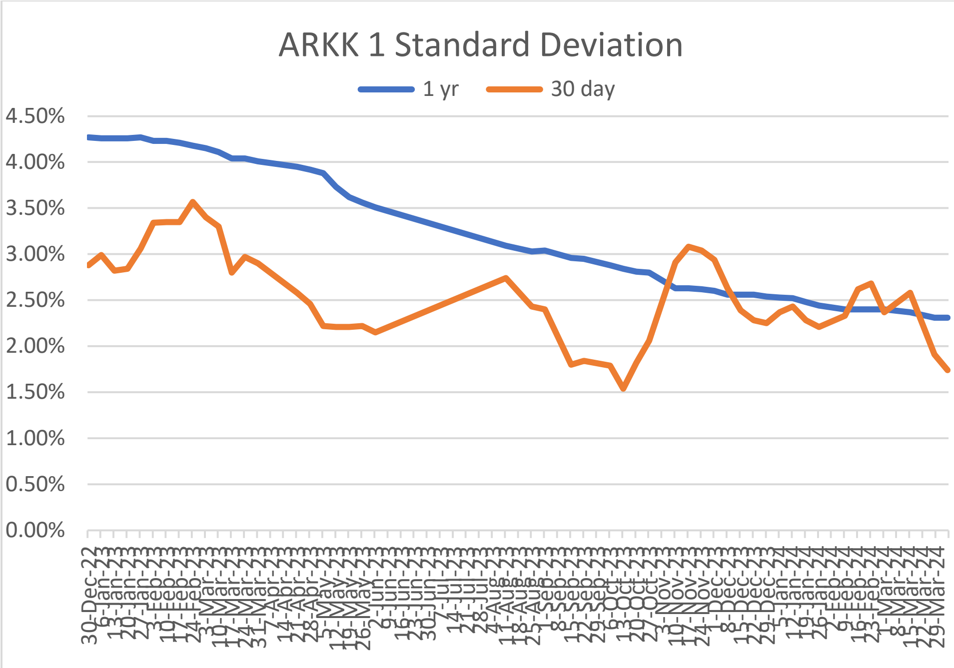
Ultimately, we think the modest selling in equities was old-fashioned profit taking. Positioning is crowded again, so an uptick in the Vix is par for the course (Volatility and selling create a vicious cycle). But to be fair, the speed at which the narrative has changed is a slight concern. Just a week ago, the market had reverted back to one of its old mantras: Strong economic data was good for equities but bad for bonds. But now strong economic data is dashing the rate-cut hopes of equity investors. However, the ultimate signal might be that the bond market actually *rallied* when equities were getting spooked. Some of this might be attributed to a "flight to quality" bid stemming from the fear that Iran might retaliate against Israel imminently. But it more likely tells us that the economic growth trajectory is not out of whack.

- Volatility divergences mean it is not interest rates

We have noted the uptick in Volatility. As you can see, it is minimal yet noticeable in the S&P 500 (SPY). This is true for the 1-year measure as well as the 30-day. But if you look at the junky companies, the ARKK Volatility has continued to grind lower. In fact, the 30-day measure is not just grinding but accelerating lower. We think this supports our theory that interest rates are not moving the market. If there were real fears of interest rates moving higher, the junky companies that rely on lower rates would surely be suffering…or at least their Volatilities would be moving higher.

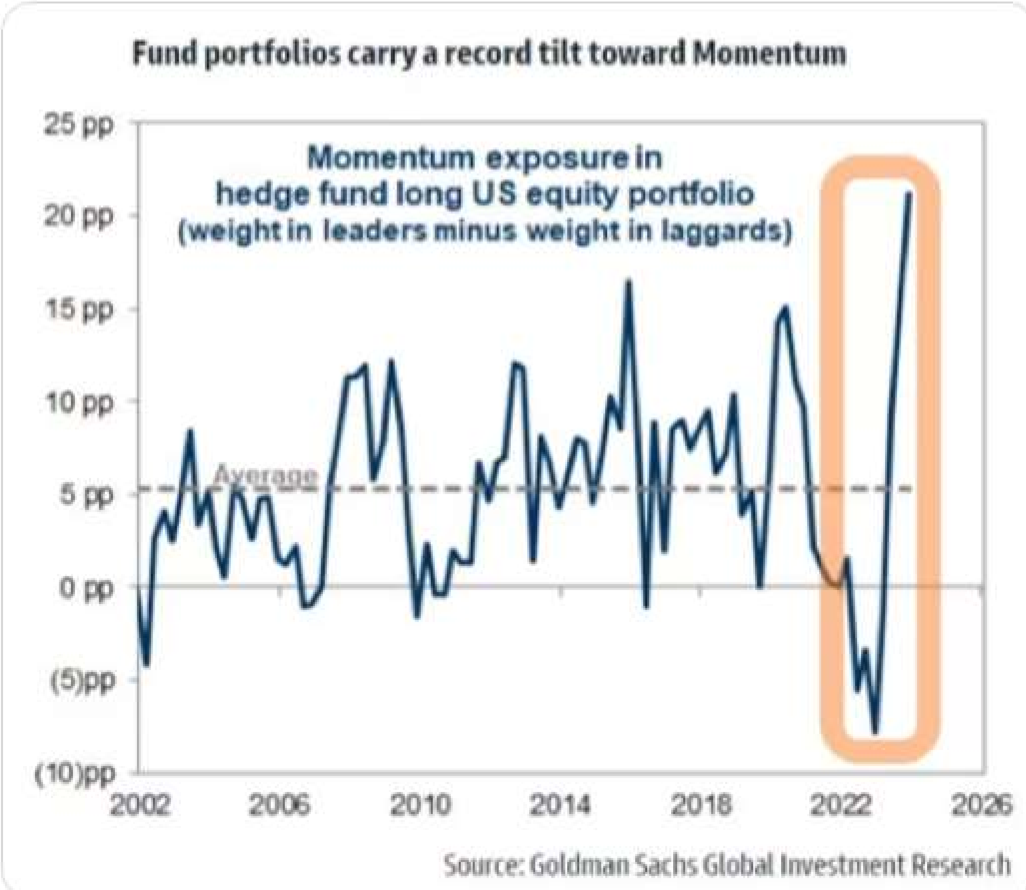
The data below is based on actual moves in the market. The Vix measures Volatility looking at option prices.





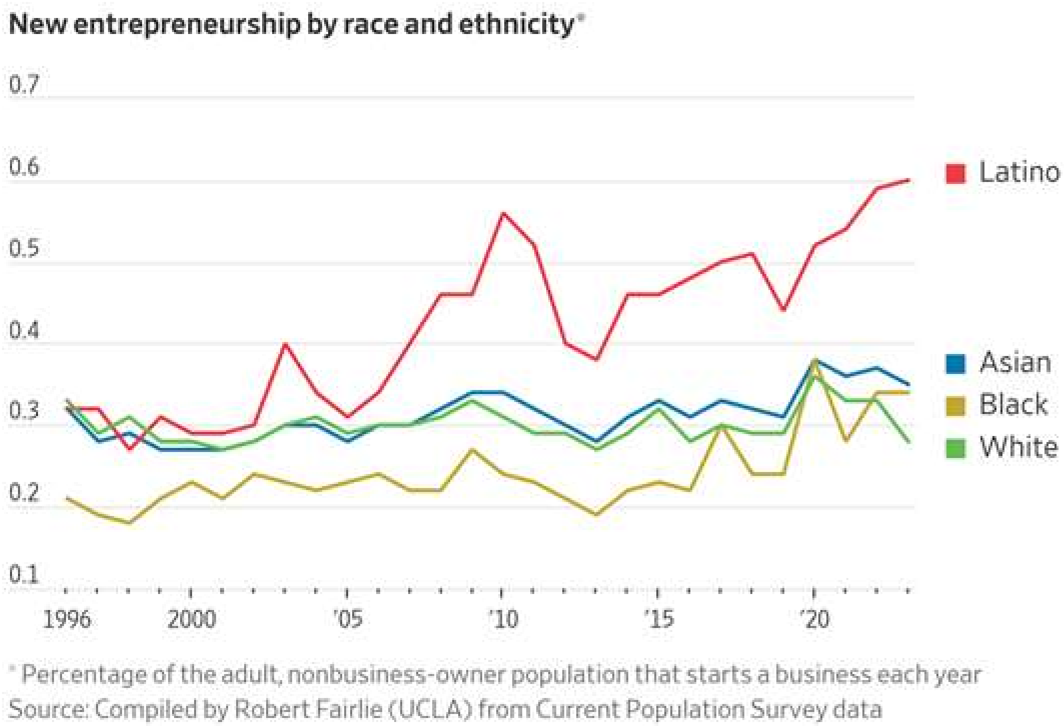
➢ Positioning is stretched, but exactly what positioning?

Here is an updated chart that we use periodically. It is Goldman's view on the crowdedness of Momentum in hedge fund portfolios. We believe it on the surface. But we also know Momentum as a factor is nebulous…its components are always changing. Moreover, it does not appear that Goldman includes short exposures in this chart. In other words, we do not put a lot of weight on it. But we do think investors are bullish and some profit taking is natural.



- Random chart on entrepreneurship by race

This might be a chart crime given the tiny increments on the y-axis. And we are not sure what to make of it anyway. But we do find it interesting.



- Inflation cools a touch, but the forward math is tough

The Personal Consumption Expenditures Price index (aka PCE inflation, the one the Fed watches the most closely) in February grew 0.3% vs January. This is marginally better than the 0.4% growth in prices in January. This is a 2.5% increase on the year. The Core PCE increased 0.3%. The annual number was 2.8% which is down from 2.9%. Goods prices (+0.5%) accelerated more than Services (+0.3). Nondurable Goods (+0.7%) led Durables (+0.2%). Food prices barely budged (+0.1%). Energy (Goods and Services) was the big gainer (+2.3%).

Five-year Inflation Expectations dropped from 2.9% to 2.8%. The one-year dropped from 3.0% to 2.9%.

Despite the positive drifts in inflation (positive being lower), some math is stacked against us. Bianco Research tells us that the base effects of inflation will get more difficult. This is the simple math when the higher monthly data from a year ago rolls off. Even with lower monthly readings now, the annual rates could move higher.

These are good numbers, but Personal Income also slowed to 0.3% down from January's 1.0% gain (which was abnormally high). And yet Personal Spending accelerated to 0.8% from 0.2% in Jan.

We are formulating a theory on the divergences and convergences of Income and Spending. Obviously, these numbers will oscillate month to month. But in the early days of Spending outstripping Income, the market does well. The immediate impulse of the Spending carries the day. But as time goes by, the gravity of lower Income swings the balance the other way.

This chart is a little confusing (hopefully not a chart crime). And we only started it in mid-2021 because there was too much noise in the data before this (Covid craziness). But when the blue line (Spending) is above the red line (Income), the market does well (green line). We need more data, and the lag effects could be tricky to monitor. But we think this could be helpful.

- Manufacturing picking up steam, Services Prices cooling

One of the headline numbers during the week was the stronger than expected ISM Manufacturing PMI. It hit its highest level in 17 months registering 50.3. New Orders were strong (51.4 vs 49.2 last month) as was Employment (47.4, still below breakeven). The strongest component was Prices which hit 55.8.
The S&P Manufacturing PMI slipped a bit in the month. 51.9 is still a decent reading. This contrasts with our view that the US economy is better than the rest of the world. (ISM is more representative of large-cap multinational companies vs S&P which is more US focused across different sizes.)

But Services are a different story. Both the S&P and ISM fell in March vs Feb. They are still at decent levels (51.7 and 51.4). Prices for ISM Services was the standout at it dropped from 58.6 to 53.4. This relieves a lot of anxiety stemming from the Prices for ISM Manufacturing.

Construction Spending in February was negative for the second month in a row. Before this mini-streak, the last negative patch was in late 2022. Private residential construction was the strongest with a 0.7% gain. Inside of this, single family building rose 1.4% vs a contraction of -0.2% in multifamily. Public residential spending fell 1.2%. Private non-residential spending dropped -0.9%. Public construction (non-residential) fell 1.2%.

The Kansas City Fed's Manufacturing index followed the Dallas and Richmond Fed's readings from last week as it sank further into negative territory.

- Employment continues to stabilize (even with fake data)

Job Openings in February per the JOLTS (Job Openings and Labor Turnover Survey) were flat vs January. This is still the lowest number in three years. And we maintain that loads of these job listings are fake news (duplicates, stale, or just fake). That said, the rate of change has flattened out. And the outright level is still 1.5mm more Openings than pre-Virus Fear. The Quits Rate has stabilized, also.

ADP's guess at the March Private Payrolls number was a strong 184k new jobs. February was 155k and the consensus guess for March was around 150k. Leisure & Hospitality were big gainers. Large companies hired more than smaller ones. Another interesting data point is the jump in pay for Job Changers (just what it sounds like). Annual compensation moved higher by 10% vs 7% last month (biggest jump since July of last year). The industries that led this jump in pay were Financial Services, Construction, and Manufacturing.

Basically, we think a lot of the labor data is misleading if not fake, but the employment situation has stabilized from the deterioration seen in 2022 and into 2023.

We will see if this trend continues with the March Employment report on Friday.

- ➢ Other economic data is mostly better
  - The final revision on 4Q2024 GDP showed growth of 3.4% (this is the annualized growth of Q4 vs Q3). The PCE inflation for the quarter (more below on February data) came in at 2%. This is old data, but it is still noteworthy that inflation hit the Fed's target for two quarters in a row.
  - Pending Home Sales in February increased 1.6% which is a nice snap back from the 4.7% drop in January. This was another datapoint (the January slump) that the market blamed on the weather. We were skeptical at the time (just like the drop in Retail Sales), but the bounce back appears to support this. (We also recently saw that some were blaming the weak January on lower tax refunds…we have not seen the data so who knows.)
  - University of Michigan's Consumer Sentiment ticked higher. It is near a three-year high. Inflation drives this survey.
  - The weekly Redbook retail sales accelerated to a gain of 5.2% vs the recent readings in the 3-4% range.
  - Factory Orders climbed 1.4% in Feb vs last month's drop of 3.8%.
  - Total Vehicle Sales in March dropped to 15.5mm (annualized run rate) vs 15.8mm in Feb.
  - The weekly Mortgage Applications slipped modestly.

- ➢ China is finally stabilizing (for now)

The official government Manufacturing PMI for March moved back into positive territory (50.8). This was its highest level in 13 months. Services also shot higher to 53. This was the highest reading since June of last year. The private Caixin Manufacturing PMI also moved higher. We know not to believe actual datapoints from the communists. But we do think the direction of the data is a decent indicator. As we have been saying, we think China has stabilized a bit…for now. We still do not want to bet on a country run by a man guided by a "common prosperity" goal. But we will take the uptick in aggregate demand to help support the global economy.

- ➢ Even a Fed Hawk and Dove agree

There have been too many Fed Speakers to recap. But the most interesting observation is the conjoining of Laura Mester and Mary Daly. These two have been at opposite ends of the Hawk (Mester) – Dove (Daly) scale. But now they both see three cuts this year as the right recipe. There are still the outliers on both sides (Kashkari and Goolsbee), but we think if these two share the same opinion, then there is probably a strong consensus on three rate cuts.

- ➢ Oil breakeven prices are going higher

The oil & gas sector in Texas (and surrounding areas) showed little to no growth in Q1 according to the Dallas Fed. Oil production fell modestly. Gas production collapsed (going from +17.9 to -17.0 with 0 being neutral).

Costs went up across the board. Most notably, breakeven prices have moved higher. Last year, $62 per barrel was the price companies needed to make a profit. This year, it has moved up to $64. This price point is not uniform. Large companies have a huge advantage over smaller ones. To cover operating costs (not a pure breakeven price), large companies need to hit $26. Smaller ones need $44.

Respondents expect oil to be about $80/barrel at the end of 2024 ($82.50 during the survey). They expect natural gas to be $2.59/MMbtu ($1.44 during the survey).

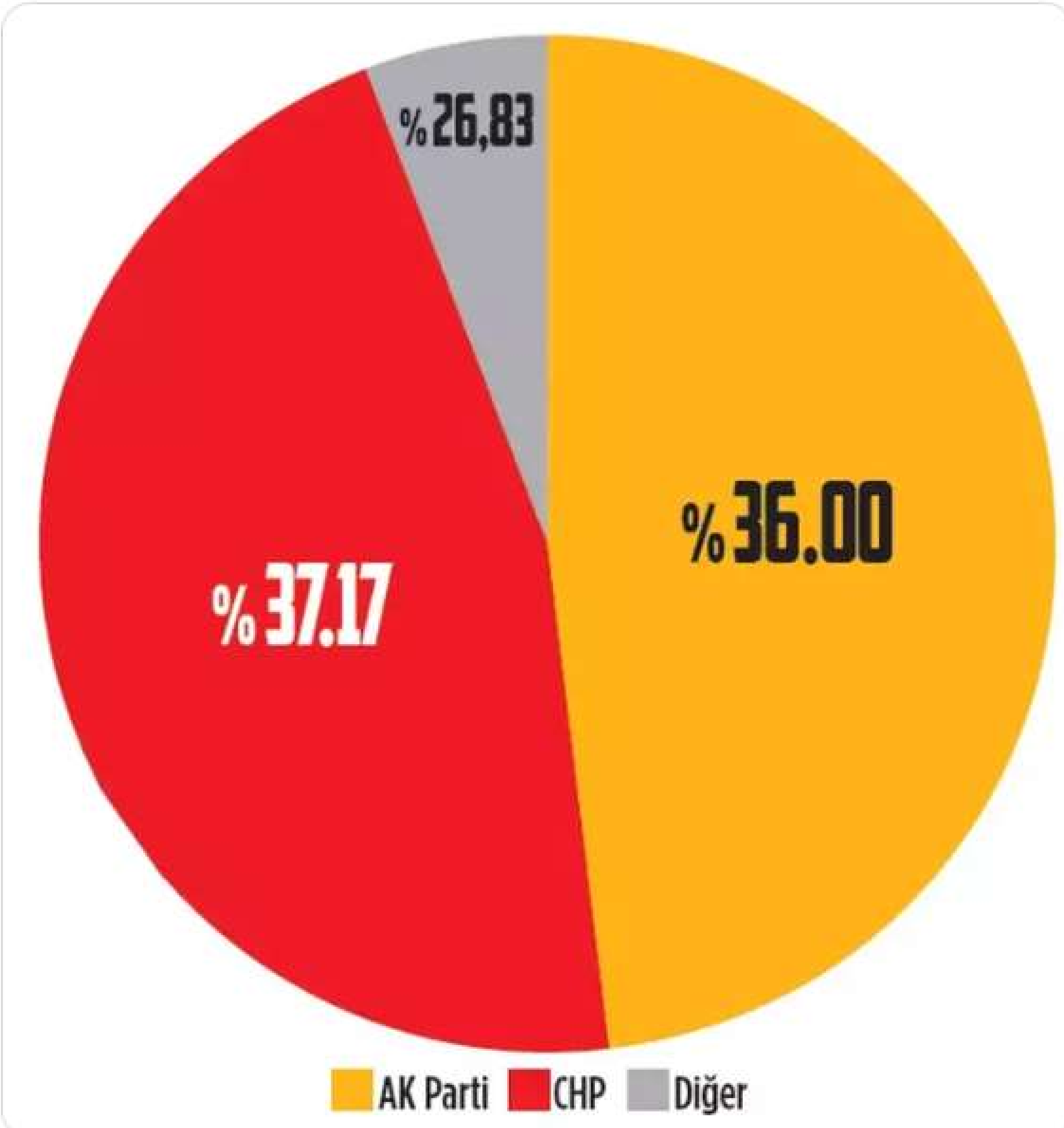
(The Dallas Fed conducts a quarterly survey with about 150 firms in the oil & gas sector. About 2/3 of the respondents are in exploration & production and the remaining 1/3 are in oil services. It is a diffusion index that oscillates around the breakeven level…similar to the broad business surveys).

- Where did all the crypto money go?

This one combines old school fraud with new school money laundering. A woman in China scammed 130,000 investors out of nearly $2b in a "wealth management" scheme. She just stole the money. But when the communists got wind of her crimes, she bolted for England. She had converted the money into Bitcoin as one cannot just freely convert CNY (the Chines currency) into other currencies. When she arrived in England, she enlisted a friend to convert the 61,000 Bitcoin back into "straight cash homey." The friend claims she did not know the funds were from illegal activity. The original thief is on the run again. The money launderer was left holding the digital bag and has been found guilty.

- Chart Crime of the week

This one is from the Turkish media trying to show the breakdown of the political parties. Perhaps there is some bias being shown in favor of President Erdogan's AK party which just lost an important local election in embarrassing fashion. As a reminder, Erdogan thinks interest rate hikes cause inflation. And he believes in e.s.p.



- Quick Hits
    - Amazon's "Just walk out" grocery checkout is not powered by AI but rather cameras and 1,000 people in India.
    - "Journalists" flying on Air Force One have been warned to stop stealing souvenirs from the airplane.
    - Canada Goose, the parka maker, has closed its Aspen store and is opening one in Hawaii.
    - The MTA (the NY authority that runs the subway and other NY-only tolls) is demanding that the NYC Marathon organizers pay it for lost revenue due to the Verrazano bridge being closed to cars during the race.
    - The Verrazano tolls collect $750k a day according to the MTA.
    - The WSJ reports that the company Super Micro is more commonly known as Supermicro.
    - California has run out of money for its shark detection system.

- One of the earliest documented uses of a mechanical bull for entertainment purposes was in New Jersey in the 1930s. (Chalk Creek Junior was curious about Mickey Gilley, so down the rabbit hole we went.)

Trading: We added to some of our long Big Tech exposure during the softness. We cut some of our Health Care as we have been leaning. The bad news just keeps piling up on different industries within the sector. We added to some Consumer Discretionary longs. We are still waiting to add shorts. And we will not add too much on the long side unless the pullback gets extended (with no new news, needless to say).

TSLAQ: Tesla whiffed on its Q1 deliveries. The total was 387k cars. The car company delivered 485k cars in Q4 of 2023 and 423k in Q1 of 2023. After many revisions downward, estimates were still around 450k. The most bearish analysts on the street were expecting 420k. Just as we have been saying, the recent April price hikes were a sign that March deliveries were a disaster. And continuing its theme, the company continues to produce more cars than it can deliver (434k produced). And the outlook is not looking any brighter. Xiaomi is the new kid on the block in China. Its entry car is $4k cheaper than the Model 3. And its backlog is stretching (but it is in the early days of production with low nominal numbers). Perhaps the notion that Tesla does not actually own its factory in Shanghai might be acknowledged by the fanbois (it has been fully disclosed in the company's 10K filings…if production targets are not met, the communists get the factory.)