Chalk Creek Partners LLC

Registered Investment Advisor

Weekly Update 16-September-2020

Carlisle C. Wysong, CFA *Managing Partner*

- Market levels off but sits precariously
- Merrill sees signs of a sector rotation
- Total Unemployment Benefits still running high: Thanks California
- Other Economic Data is mixed
- The Fed holds the line and keeps rate expectations anchored at 0% until 2023
- Add some Vomma to your Gamma
- Conflicting supply/demand issues in crude oil
- Chart Crime of the Week
- Click here for the full note

	Last	5d %	YTD %	1yr %
SPX	3385	-0.4%	4.8%	12.9%
QQQ	274.6	-1.2%	29.2%	43.3%
US 10 YR	0.69%	0.70%	1.88%	1.80%
VIX	26.0%	28.8%	23.2%	14.4%
Oil	40.25	5.8%	-34.2%	-36.2%

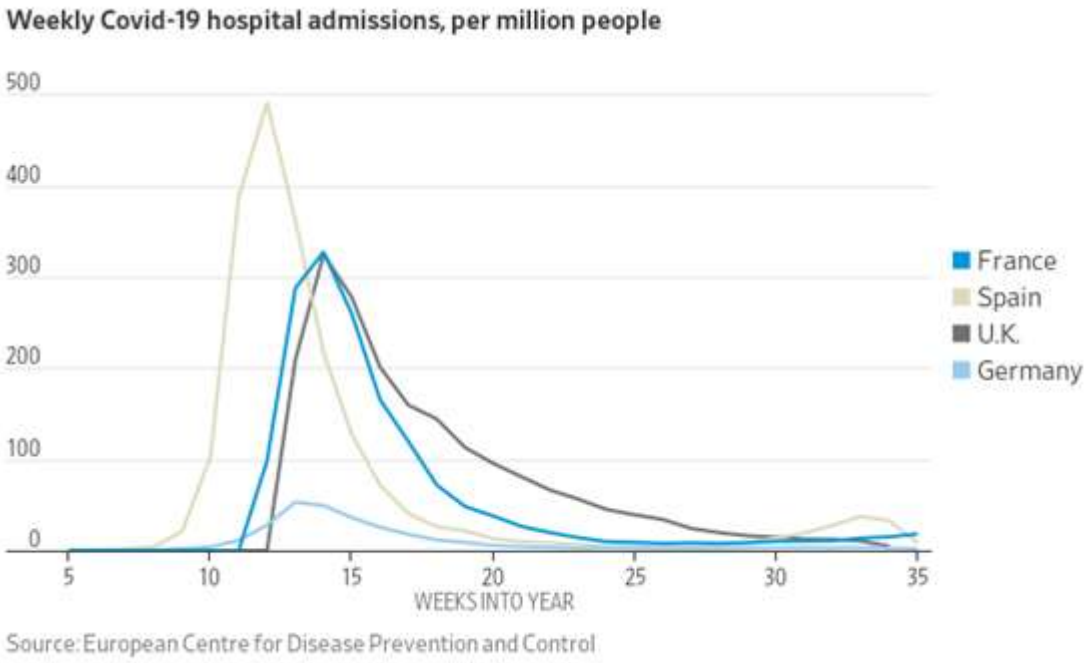
*10yr and VIX are levels not changes

** Oil is front month futures, beware

The market leveled off after last week's weakness in Big Tech and the other speculative parts of the market. Volatility on the surface has dipped, as well. But it remains elevated within different sectors and factors. The virus and the hopes for a vaccine still control much of the day-trading. Economic data is still surprising on the upside, but the employment situation does not seem to be getting better. The hopes of another round of fiscal stimulus (handouts) appear to be improving. One area of the market to monitor closely is the calendar of IPOs. They are starting to come fast and furious with some silly valuations. Never a good sign. Alas, the Fed is still backstopping this market.

Some Democrats and Republicans have created a bipartisan group aiming to get a new stimulus program. They call themselves the "Problem Solvers" caucus; they are pushing for a" skinny" stimulus package which the Dem leadership has previously rejected. Without getting caught up in the deeming of a $1t package as "skinny," it appears as though both sides are beginning to find some common ground. As much as we hate runaway deficits, another round of stimulus might help keep the economy chugging along.

For what it is worth, we are not overly worried about the infamous "second wave" in Europe. Below are some of the hospitalization rate. Of course, not everything is rosy as Ireland has declared a second lockdown after a large increase in deaths. Nonetheless, we are optimistic.

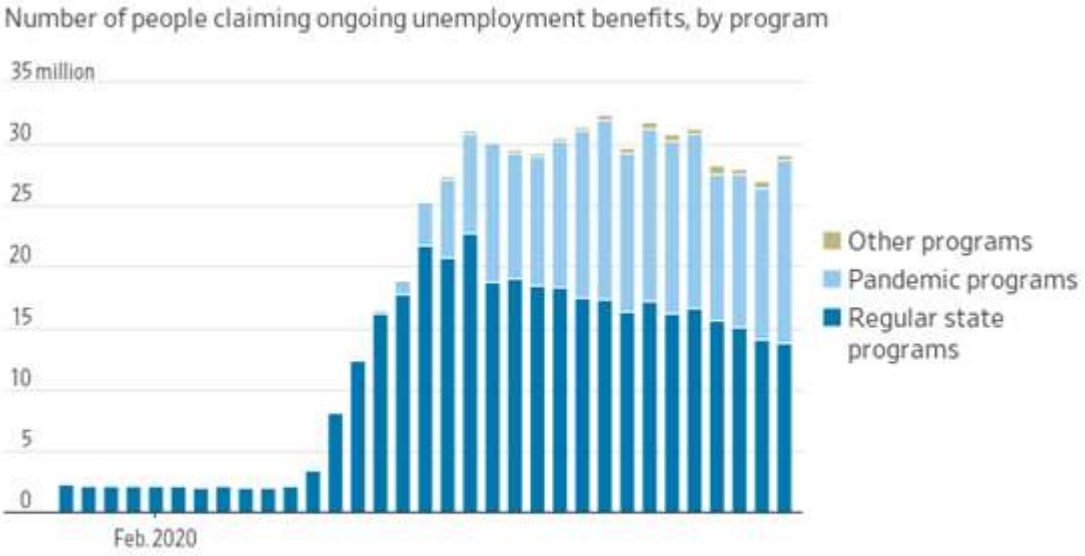


- Merrill sees signs of a sector rotation

Merrill Lynch's Fund Manager Survey showed mostly unsurprising results. Big Tech and Healthcare remain the most overweight sectors. But investors have started to trim these longs. They have rotated to Industrials and Small Caps with the hopes of catching a Value rally. But Cash levels* have increased. And, of course, Financials and Energy are still universally hated (and this is why we have to own some of each). Separately, ML's analysis of client activity showed Hedge Funds and Retail bought the Big Tech dip while traditional institutions (like mutual funds) were net sellers. We generally agree with the rotation theme from a tactical point of view. Or rather, we believe in a little more balanced portfolio in the short-term rather than all Big Tech all the time.

- Total Unemployment Benefits still running high: Thanks California.

Initial Jobless Claims changed zero from last week registering at 884k again. Other than this being a little weird (literally not changing), it shows the employment rebound is stalling. Moreover, the total Continuing Claims through all the programs (state and federal) moved higher to 29.6mm. We acknowledge these numbers continue to be muddy with the change in methodology and the potential double counting for back-dated claims. But there is also California. It accounted for 3.9mm of the 3.6mm jump in federal unemployment claims (yes more than the total)! Part of this might be backdating. Part of this might be fraud. But part of this is most definitely an economy that stinks. Here is the combined benefits chart we keep posting:



Note: Pandemic programs include Pandemic Unemployment Assistance and Pandemic Emergency Unemployment Compensation
Source: Labor Department

- Other Economic Data is mixed

  - Housing Market Index hit an all-time high. (+)
  - Monthly disinflation (a slowing rate of inflation, not negative) outweighs an increase in annual inflation (AEI told us to look at the recent trend). (-)
  - Mortgage Applications fell in August after a head-fake higher in July. (-)
  - Retail Sales a little light. Non-store sales…that is e-commerce…increased 22% in August vs last year. (+/-)
  - Industrial Production has leveled off. (-)

- The Fed holds the line and keeps rate expectations anchored at 0% until 2023

The Federal Reserve Open Market Committee (FOMC) left the Fed Funds target interest rates unchanged at 0% (technically the range is 0%-0.25%). The real story, which is not new either, is that the Fed reinforced its new policy of ignoring inflation for the sake of job and wage growth. Rates will be lower for longer (as they say). The market reaction was a bit perplexing on the surface as Big Tech sold off while the rest of the market was more resilient. But this actually makes sense. If the Fed really is hell bent on bringing about inflation (we are happy to argue the merits of this policy in general), then the "long duration" assets like growth stocks should underperform. We think our opinion is more nuanced than this in that quality growth names are not reliant upon a zero interest rate environment. And the notion that we will have run away inflation any time soon seems outlandish, too (but we do think there will be inflation with all of this profligate, government (redundant) spending. But not in the short to medium term. But we digress).

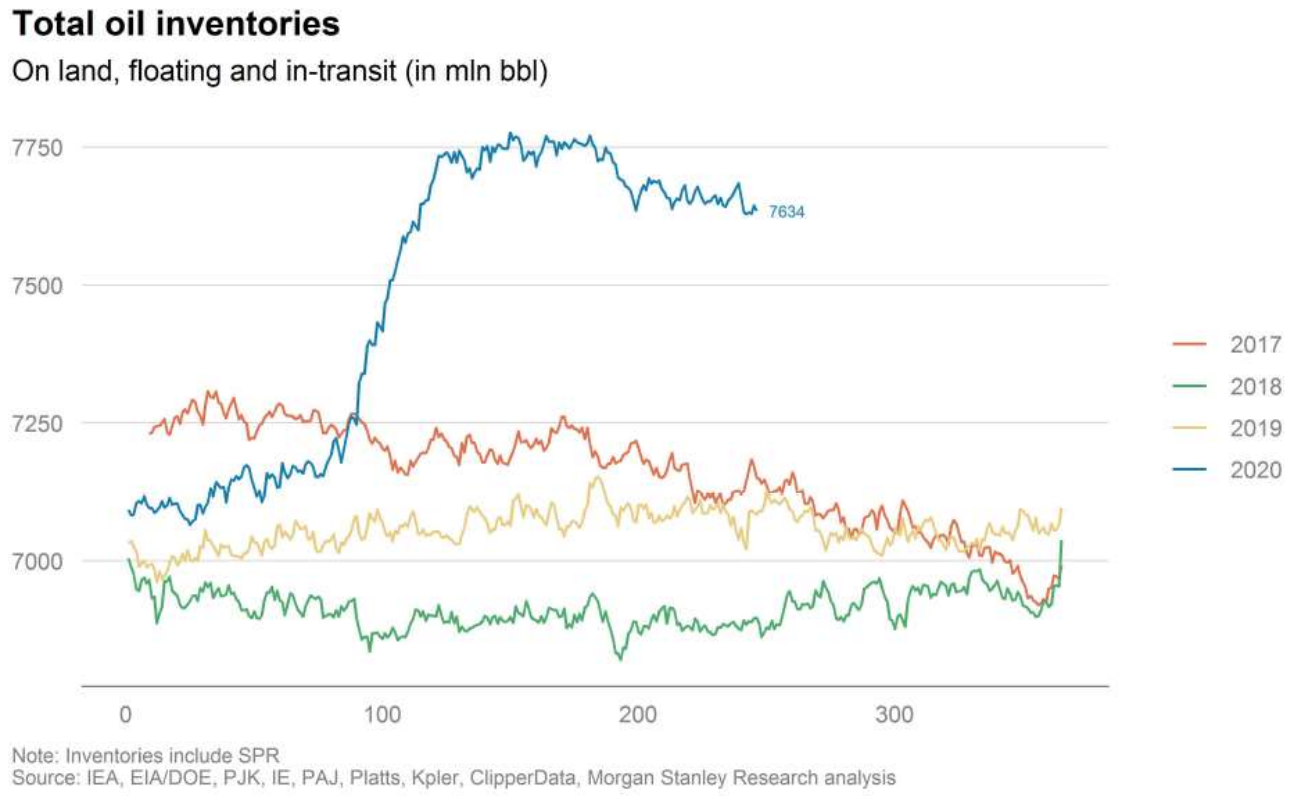
Japan has a new Prime Minister, Yoshihide Suga**. He is the outgoing PM's righthand man, so there should not be any disruption in the "Abenomics" policy. Moreover, he thinks monetary policy coming from the Bank of Japan (the central bank) should be even "easier" – he wants to pump more money into the system.

- Add some Vomma to your Gamma

Here is another one for the math-geek files – so jump ahead to oil if you are not in the mood. There has been a ton of talk about Gamma and its impact on option prices. Recall, Gamma is the second derivative impact on option prices. If we think of Delta as the *speed* at which option prices change relative to the underlying asset price, Gamma is the *acceleration*. Similarly, Vega measures the impact on option prices relative to the changes in Volatility. Vomma is the second derivative of Volatility. Another way of saying this is Vomma measures the Volatility of the Volatility. Vomma just happens to peak at the same levels where many of the maniacs were buying way out-of-the-money Call options. The sellers of these options (market-makers) had to deal with the Gamma and Vomma kicking in. Again, they had to buy high and sell low.

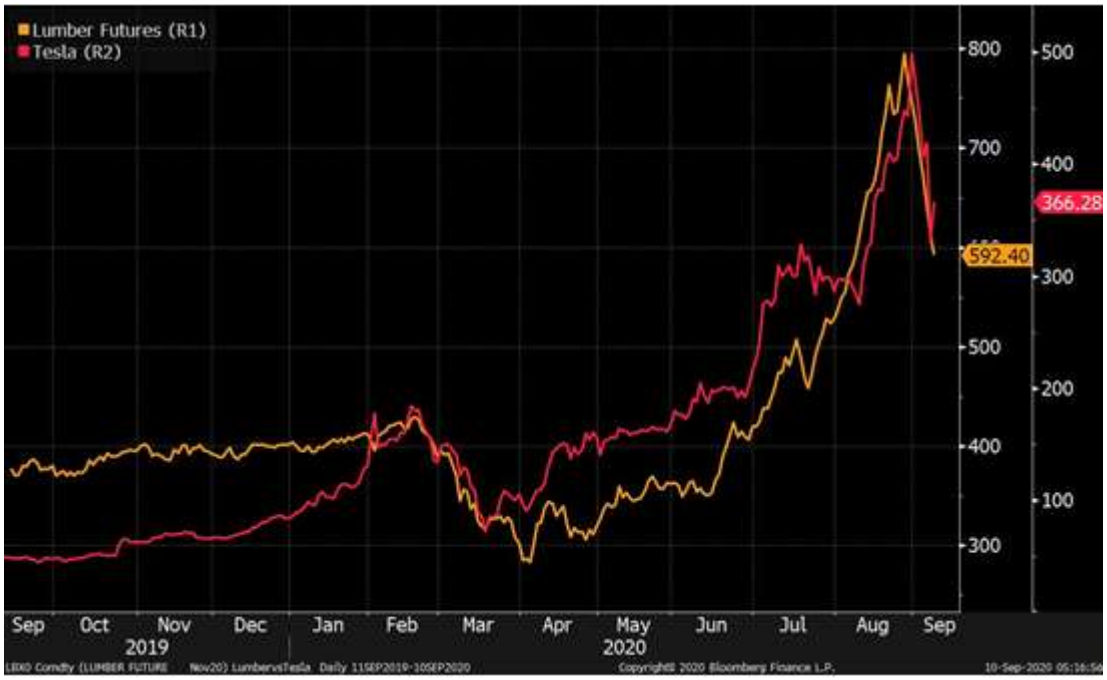
- Conflicting supply/demand issues in crude oil

Iraq joined Saudi in slashing crude prices. This is obviously a response to decreased demand. China is the exception – it is still reporting increased demand. At best, the weakened global demand picture outweighs the Chinese demand. At worst, the Chinese are lying about demand and have just been buying oil and parking it in offshore tankers. Here is a snapshot of total, global inventories (courtesy of Yahoo Finance which can be a good resource surprisingly). But this picture has changed in the last two days. There was a large, unexpected draw in US inventories. We continue to believe that oil will stay range bound oscillating around the $40 level.



- Chart Crime of the Week

Bloomberg thought it would be cute to overlay the chart of lumber with that of Tesla. In one of the go-to crimes, they used different y-axes. Lumber is up about 50% in the chart. Tesla is up over 800%. Not exactly "similar" as Bloomberg put it.



- Quick Hits
  - Jacksonville Jaguar tickets are selling for $28.
  - Texas A&M tickets are selling for $400.
  - Ad prices for NFL Sunday Night Football are up over 30% vs last year.
  - Thursday and Sunday night's NFL viewing audiences were down about 15% vs last year.
  - 6mm Americans will bet on the NFL with a bookie this year.
  - Many Robinhooders are unaware they must pay taxes on capital gains made via stock trading (according to the WSJ).
  - Vinyl record sales have surpassed CD sales this year.
  - Turkey has imported $15b worth of gold so far this year. This is up 153% vs last year. The Turkish Lira is down over 20% vs the USD this year.
  - The Chinese communists have pushed local banks to extend loans to hog farmers to combat a shortage of pork. These hog loans are to be backed by the shrinking hog herds.
  - Asian airlines are conducting "flights to nowhere" which depart and arrive at the same airport.
  - A "gender reveal" party with fireworks is responsible for one of the wildfires ravaging California.
  - An Austrian man set the world record for being submerged in ice up to his neck: 2.5 hours. No word if he jumped in a Finnish sauna afterwards.
  - A fraud prevention startup called NS8 had to fire hundreds of employees for…fraud.
  - Research shows that red-light cameras reduce cross-road collisions but increase rear-end collisions.
  - The billionaire who created Duty Free shops has fulfilled his pledge of giving away all his wealth. His foundation has given away $8b. Chuck Feeney and his wife left themselves $2mm for retirement.

*There is no such thing as Cash "on the sidelines!" See the Jargon section of the website for the rant.

** The only suggested person from a Suga google search is for a South Korean rapper.

Trading: We are still conflicted in our market view. The economic damage from the lockdowns will be long lasting. Of course, the Fed's action will be long lasting, too. They have said as much with their new view on inflation (better to overshoot than to stifle labor growth). The swing factor might just be fiscal stimulus. It has undoubtedly been a boon to the economy and the markets. But its limits are likely to be reached very soon. This leaves us with pretty much the same market positioning. We like Big Tech for the long haul, but we have hedged a lot of the exposure in the short term. We mostly like Quality stocks (high Return on Equity or Invested Capital, solid mgmt., stable earnings/cash flow), but we have mixed in some Value names. We are still evenly split between Work-From-Home stocks and Recovery stocks. We still like Gold as a long-term hedge to USD erosion (brought on by the extreme fiscal and monetary policies). We have cut back some of our Trading positions while increasing some of our defensive names.

TSLAQ: Another mini-bubble seemingly popped this week: Nikola (NKLA). The EV truck maker that has never made a truck was called out by a short-seller for fabricating its technology and everything else relating to the company. The fact that a company with no revenues was worth about $35b pretty much sums up the insanity. Hilariously, the twitterverse rumor is that Elon Musk is behind the short-seller research. There can only be one charlatan in the EV space! We bought Puts once the story broke. We do not typically like shorting into weakness (share price sinking and Volatility spiking higher which means options are more expensive). But when the specter of bankruptcy is real, it is worth a punt. As for Tesla itself, it is having a manic rally into its Battery Day even next week. This will likely be a classic buy-the-rumor and sell-the-news event. We sold some of our Tesla Puts early in the week for a nice gain. We will look to add this back when the fluff gets extreme again. For what it is worth, Tesla is the perfect barometer ("it is called a thermometer") for risk appetite in the stock market. We are using this "factor" in our tactical hedging process.

www.chalkcreekpartners.com

Carlisle's Twitter Financial List

Carlisle's LinkedIn