Weekly Update

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- Market Rotation is back
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- Inflation is Transitory! Or so says Wall Street…but not Main Street
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- Housing is led by $1mm homes
- Business confidence is down from the October bounce-back but still strong
- Europe is improving; China is not
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	Last	5d %	YTD %	1yr %
SPX	4701	0.3%	26.4%	31.2%
QQQ	398.8	0.3%	27.5%	36.1%
US 10 YR	1.64%	1.59%	0.92%	0.85%
USD/DXY	96.7	95.8	89.9	92.3
VIX	18.6%	17.1%	22.8%	20.8%
Oil	78.3	-0.3%	61.0%	71.0%

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

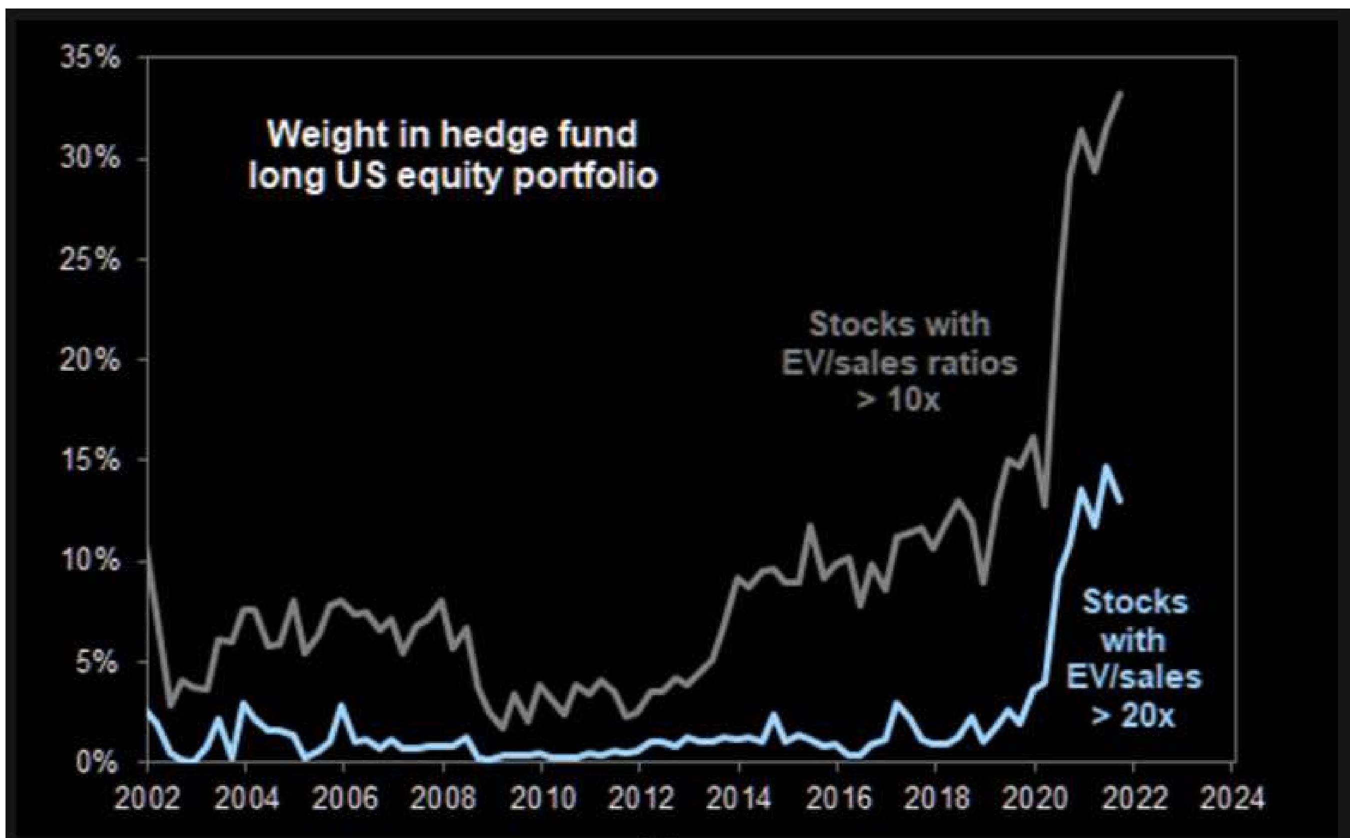
Market Volatility ticked higher on the headline indices. But the moves under the surface were much more violent. A perfect storm of shifting narratives left some carnage in the rotation's wake. This storm included a one-two punch from central banks (or at least the market's diverging views of central banks), renewed virus fear, and some nasty earnings misses. And lest we forget, hedge fund positioning was precisely wrong which exacerbated the pain.

The central bank one-two started with extremely dovish comments by the European Central Bank (ECB). Global interest rates started to compress. This coincided with the hedge funds being stopped out of their steepening

trades (forced to sell short-term bonds and buy long-term bonds). This technical reaction made investors start to doubt the current economic growth landscape. Then we got Biden's reappointment of Jerome Powell as the Fed chairman. People thought this was the bull case for the market given the removal of any uncertainty. But the market quickly turned this narrative on its head and proclaimed that Powell was going to raise interest rates after an accelerated tapering of bond purchases. The market now is assigning an 80% chance that the Fed hikes rates at the June 2022 FOMC meeting. The probability was 58% a month ago. And there is a 65% chance of three rate hikes by the end of 2022. The profitless High Growth names, the longest duration assets which rely on ultra-low interest rates to extend life to their projects, were taken to the woodshed. Moreover, revenues from most of the high-flyers are slowing. As a sign of the times, Blomberg has custom indices that track "loss-making companies."

- Positioning is the usual culprit

Goldman Sachs tells us that almost 50% of hedge fund long positions are in stocks with valuations greater than 10x Sales (the market multiple to sales is 3.2x). But in the same report, Goldman tells us that hedge funds are tilting more aggressively into Value instead of Growth. Bloomberg speculates that hedge funds are trying to hit a homerun with high beta stocks from both ends of the spectrum (low valuation Reopening stocks coupled with high valuation tech stocks) during the final stretch of the year after lackluster performance. We think this sounds about right. But to run a barbell strategy which excludes the highest Quality Growth stocks seems a bit cavalier. And they are now paying the price.



- Inflation is Transitory! Or so says Wall Street…but not Main Street

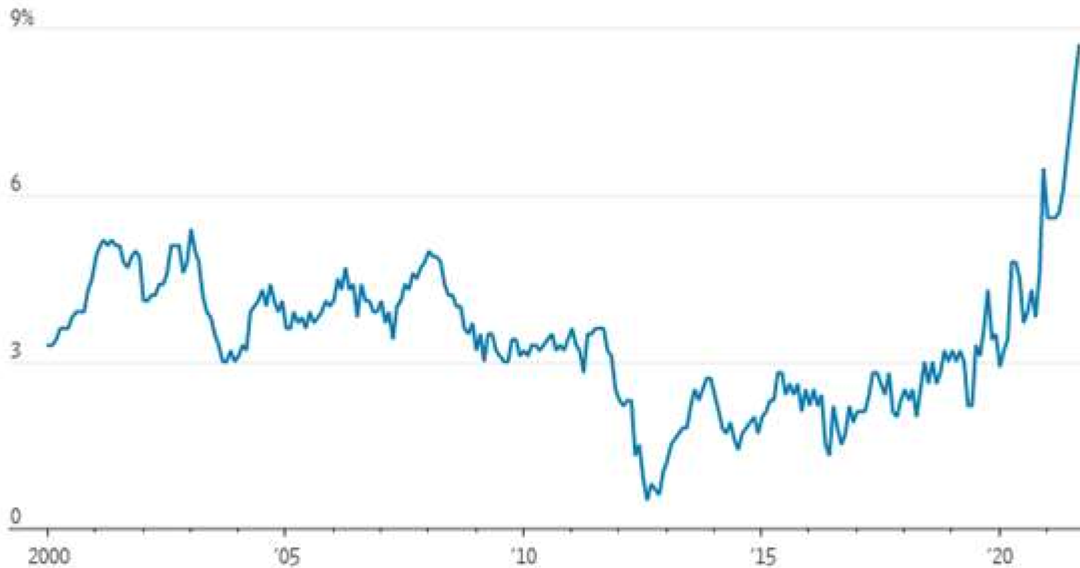
We are a little late reporting on the Merrill Fund Manager Survey from last week. But there are some noteworthy nuggets. Investors are the most bullish for the yearend run since 2013. Only 8% are underweight equities. Rates are expected to climb with stronger growth. And, yes, inflation is thought to be Transitory! This gives us some contrarian comfort in holding onto our inflation longs. Of course, Main Street disagrees with Wall Street. To wit:

Official inflation (the Fed favorite Personal Consumption Expenditures or PCE) continues to run hot. The headline increased 5% vs last year with the "Core" increasing 4.1%. Recall this measure uses business prices and not consumer prices, so it is more understated than the CPI. The good news is that Personal Incomes increased more than expected (0.5% on a monthly basis which sits right between the headline inflation rate and the "core" inflation rate).

However, we would note that shipping costs are starting to cool. Below is the Baltic Dry Index. This tracks the prices for bulk materials like iron ore, coal, and grain, so it is far from being a perfect indicator. But the number of containers sitting in Los Angeles has also dropped dramatically. And we know from the likes of Walmart and Target that many large companies loaded up on inventory earlier in the fall. No wonder there were log jams! While we think inflation will run longer than the Fed expects, we do not expect continued price surges (and certainly not hyperinflation).

- ➢ Nobody wants to be a health care worker

This chart is why we have been long health care staffing. We woulda/coulda/shoulda been much larger a long time ago! This sector is volatile despite the data going in one direction. We will try to trade around the space a bit.



- Housing is led by $1mm homes

Existing Home Sales increased marginally to an annualized rate of 6.34mm homes in October. This is up from 6.29mm in September. But it is down 5.8% from October of 2020. The Inventory of homes for sale is only 1.25mm which is down -12% vs last year. This is only 2.4 months of supply compared to the normal five to six months (this data changes based on the current run rate of Sales, so the 2.4 months is even lower when adjusted properly). The median price increased to $353,900 which is up 13.1% vs last year. Sales of homes that cost under 250k fell 24%, sales in the $750k-1mm range rose 25%, and those over $1mm increased 31%. Investors made up 17% of all buyers compared to 13% in Sept and 14% in Oct 2020. First-time buyers fell to 29% vs 32% last year with the average around 40%.

New Home Sales for October remained steady at an annual run rate of 745k (vs 742k in Sept). But expectations were for a number closer to 800k. Pricing, of course, is the culprit. The average price is up 17.5% vs last year. The number of homes sold but not yet started is starting to tick higher again. This shows builders have more confidence on the supply side (costs will not be out of control) and the demand side (home prices will stay high).

We are still sitting on the sidelines. We have been tempted to get long again. We suspect there will be another downdraft either when prices decline or the fear an interest rate hike gets even more intense.

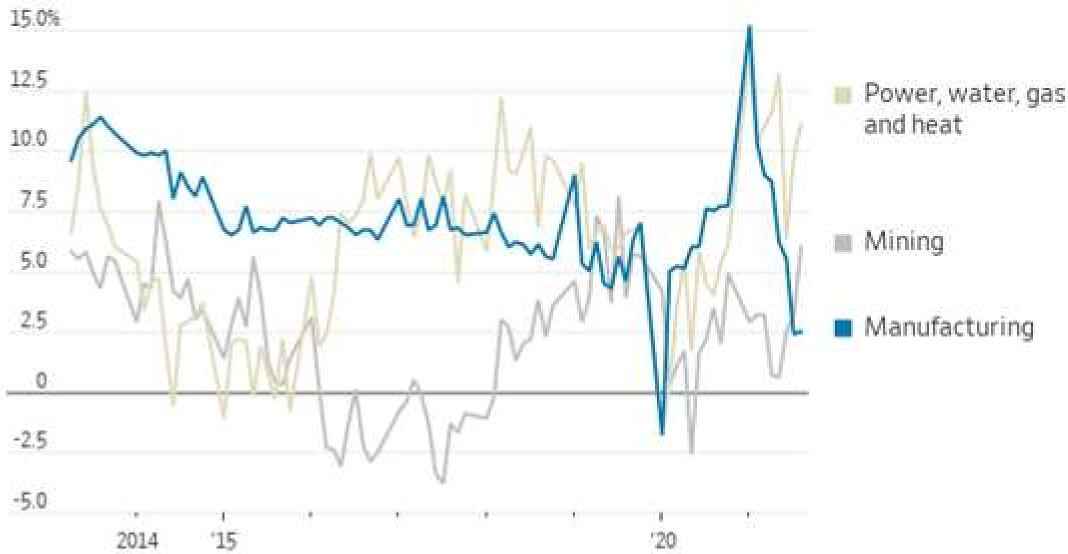
- Business confidence is down from the October bounce back but still strong

Business confidence continues to be volatile as the virus-fear moves around the country with the weather. According to the Markit PMI for November (the Flash or early read), Manufacturing remains robust bouncing back from a slight dip in October. Services slumped two points, but the optimism levels are still significantly above the delta-variant fear levels in August and September.

- Europe is improving; China is not

Eurozone PMIs are still below those in the US, but both Services and Manufacturing are trending higher.

And here is how the Chinese “recovery” is going. We used to say the communists can make their people build things but not buy things. It looks like even the first part of this equation is falling apart.



- Durable Goods slow but not for business spending

The headline New Orders dropped 0.5% in October vs September. September was also a decline. August was an all-time high, so there is no worry yet. But the trend appears to be rolling over. Of course, Autos are still a major drag due to the chip shortages. But Core Capital Goods, aka business spending, continued to increase. This has been trending higher since the beginning of the virus fear (April 2020).

- Inventories are starting to recover, sorta

Retail Inventories increased in October vs a decline in September. This matches what Walmart and Target have been telling us. Furthermore, Wholesale Inventories saw their biggest monthly builds ever (first chart). Alas, the Inventories to Sales ratio is just now beginning to recover (if you squint at the second chart).

- Other Economic numbers
  - Jobless Claims fell sharply to under 200k. This is the lowest number since 1969.
  - 3Q GDP was revised a touch higher to 2.1% growth as expected. 4Q is expected to accelerate back to the 4% growth area (big dispersion in professional guesses).
  - U Michigan's Consumer Sentiment survey for November improved from the lousy preliminary reading earlier in the month. But the final reading is still, lousy, too. Inflation is the worry, obviously.

- The new Fed same as the old Fed

The market has been focusing on whom Biden would appoint (nominate) as chairman of the Federal Reserve Board of Governors. Current Fed chief Jerome Powell was thought to be the candidate that would bring stability to the position, but obviously the market has changed its mind (at least for now…we think Powell will remain too scared to hike rates anytime soon). But maybe just as important, Biden has three more positions on the Federal Reserve Board of Governors to fill (two members are retiring and one spot was already open). We think the tradition of the chairman controlling the narrative will continue. But we think the days of the absolute control are over. However, none of this will likely matter with the new Fed. The appointees are likely to be political and thus will be biased towards not hiking rates. This is good for the short to medium-term. It just intensifies the worries down the road.

- Biden wants oil to go down, so naturally it goes up

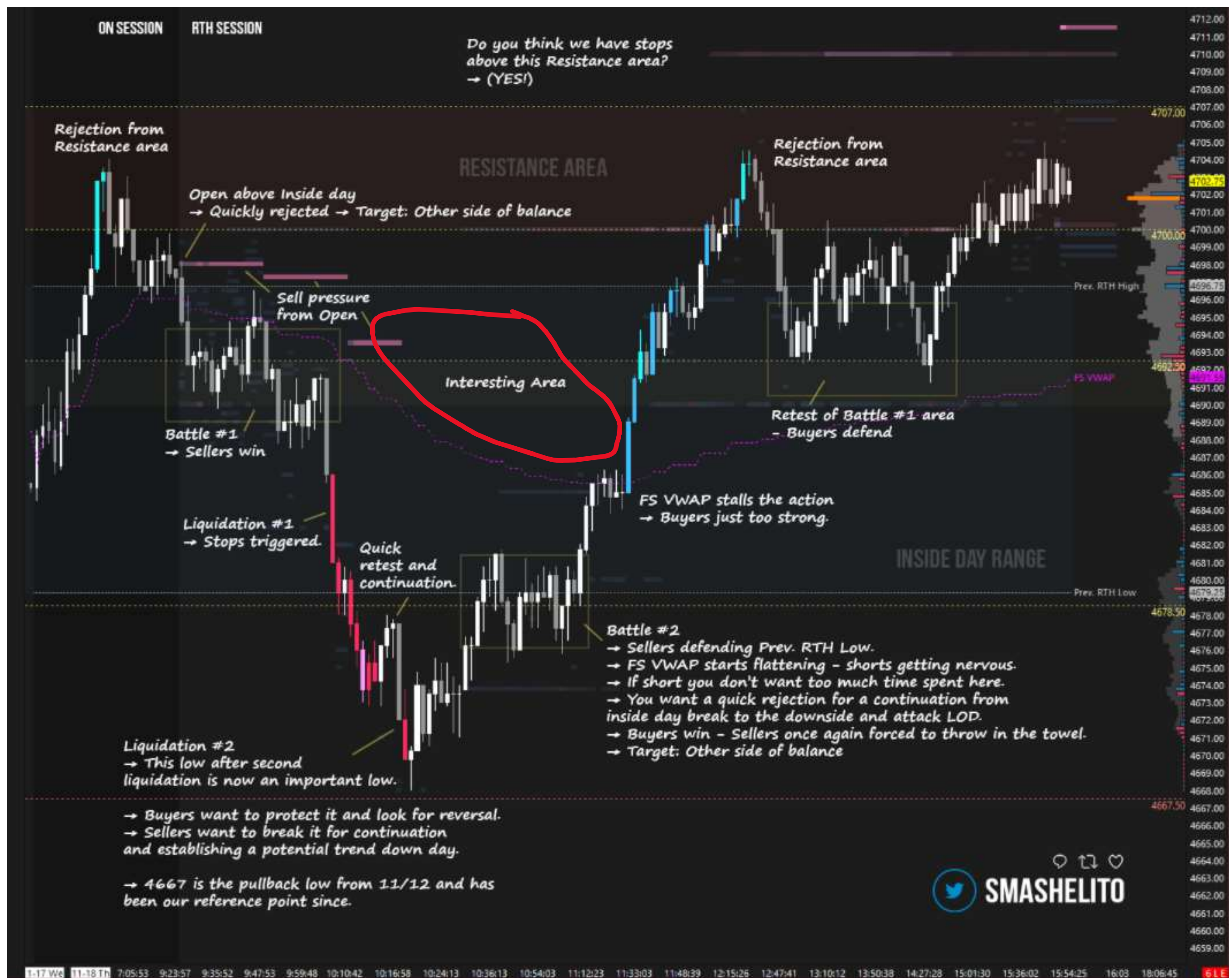
Biden announced the government will release 50mm barrels of crude from the Strategic Petroleum Reserve (SPR). We wrote that 60mm would be the maximum amount released which would barely be three days of demand. Strangely, the majority of the release (32mm out of the 50mm) will be done via swap agreements. Refineries will be forced to take crude deliveries in the coming weeks, and then they will replenish the reserves at preset times over the next two years. Despite the government's claim that oil will be down to $60 a barrel in 2022, the refineries will obviously buy futures to offset any risk: The refineries are taking oil worth about $80 and are buying futures around $65. It is more complicated than this, but the point is this political action is meaningless for the real value of crude. The other 18mm barrels will be sold directly into the market in mid-December. This is less than one day's worth of demand. Actually, most of this oil will be exported because the SPR will be releasing sour oil (and not sweet) which is more expensive to refine in the US.

It is worth noting that the US government has been releasing oil from the SPR since April. The SPR was meant to relieve short-term production disruptions (or foreign supply disruptions back when the US was more reliant on foreign oil). Needless to say, these small amounts cannot change the laws of economics (supply and demand) in the medium-term (not to mention the long-term). Naturally, the price of oil rallied on the non-news.

China, Japan, India, South Korea, and Great Britain will also be releasing oil from their own reserves. The exact amounts are unknown except for India: 5mm barrels. And OPEC+ might react by not following its predetermined path to increase production by 400k a month. We are still long Energy stocks and might be adding to our positions.

- Chart Crime of the week

This chart is probably too difficult to read. You will be better off without it. If only these geniuses could give us all these areas and points ***before*** they happen! But we do love the middle portion of this ***one-day chart*** labeled the “Interesting area.”



- Quick Hits
    - Bitcoin and Big Tech have a correlation of zero according to Bloomberg. This is down from 0.55 just two months ago.
    - CALPERS, the US's largest pension fund, recently decided to use leverage to boost returns. Uh-oh.
    - The Green Bay Packers are selling stock for the sixth time in their history. The offering consists of 300,000 shares at $300 per share ($90mm). 5mm shares are outstanding before the new equity. The stock does not pay dividends, no voting rights, and cannot be sold. You get a stock certificate. As an NFL owner, you are subject to $500,000 fines for any disparaging comments directed towards the league.
    - The buying of mortgages by the federal government is one of the few entities that adjusts its limit depending on where you live.
    - The start-up college, the University of Austin, has the mantra to be "fully committed to freedom of inquiry, freedom of conscience, and civil discourse." Critics are heaping ridicule upon it for being "political."
    - A professor at Old Dominion thinks we should call pedophiles "minor-attracted people."
    - The % share of TV viewing: Cable 37%, Broadcast 28%, Streaming 28%, Other 6% (like gaming and DVDs).
    - 75% of opioid overdose deaths in the US are from bootleg versions of fentanyl.
    - Biden's appointee to head the Comptroller of the Currency backtracked on her comments that small oil & gas companies should go bankrupt. She said, "My intention was…exactly the opposite."
    - Merck is being sued for its shingles vaccine. The claim is the vax causes the shingles instead of preventing it.
    - Nebraska has the lowest state unemployment rate (1.9% in October) since 1976 (the start of the data collection).
    - Soccer club Manchester City has dropped a partnership with a crypto platform after the club could not find any history of the platform's owners.
    - Mariah Carey will get paid about $2mm in royalties this year for "All I want for Christmas is you."
    - The Ontario School Teachers union has changed its rules to weight the votes of non-white members higher than white members.

Trading: We reduced a little of our long High Growth exposure. This has a tiny weighting. But we think tiny might still be too much. We replaced it with some more of our more idiosyncratic Trading names. These are mostly small-cap names with catalysts. But we also added a new Retail name that has been washed out with the Earnings destruction in the sector. We started a new Energy position. As we get more confidence, we will continue to add (we think the macro backdrop for Energy investing is great right now thanks to government bafoonery).

TSLAQ: Ever since The Bond Villain started selling billions and billions of Tesla stock, he has been pretty quiet. Then again, he cannot help himself sometimes…

At least 50% of my tweets were made on a porcelain throne

11:20 PM · Nov 21, 2021 · Twitter for iPhone

15.7K Retweets **3,296** Quote Tweets **253.8K** Likes

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