Chalk Creek Partners LLC

Registered Investment Advisor

Weekly Update 8-July-2020

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- Market keeps going, another all-time-high for the Nasdaq
- Earnings pre-announcements are less negative, maybe
- Sporting goods trend continues
- Employment bounces back strongly, but beware of the data

	Last	6d %	YTD %	1yr %
SPX	3116	1.7%	-1.9%	6.5%
QQQ	250.5	3.8%	22.3%	37.1%
US 10 YR	0.66%	0.68%	1.88%	2.06%
VIX	28.1%	28.4%	23.2%	14.1%
Oil	40.86	2.8%	-33.0%	-29.1%

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

The market continued its amazing run into and after the long weekend. Through Monday, the S&P had notched a record five straight days of at least 0.50% gains. Nasdaq was up 15 out of the last 17 days. Part of this euphoria is coming from the Chinese stock market's strong returns recently. The thought here is that if they are out of the woods, then so are we. Of course, believing anything coming out of China is foolhardy. Some are looking at Warren Buffett and Berkshire Hathaway finally putting some of their giant cash stockpile to work in buying the midstream energy business (pipelines, gathering and processing of natural gas, etc) of Dominion Energy. While the jump in virus cases is still cause for concern, the still declining death rate is providing a lot of relief.* As for the Fed and more fiscal stimulus, news was quiet on both fronts. But investors still view these two factors as the driving forces. And oddly, this is especially true if the virus impact does reverse course higher (or as we say, if the *fear* of the virus reverses back higher). The government backstop is ever-present.

- Earnings pre-announcements are less negative, maybe

It is early in the earnings season, but a noticeable trend is developing. The balance of corporate pre-announcements is almost equal between negatives and positives. Typically, negatives outweigh the positive about 3:1. We have discussed this before: companies always want to under-promise so they can over-deliver. Obviously, there are the pre-announcement blow-ups. But the vast majority are model tweakings. But this quarter, the ratio of negatives to positives is only 1.3. We suspect the data might be skewed because of the higher number of companies that have withdrawn guidance. It stands to reason that if a company were clicking through the virus times without any hiccups, then there would be no need to pull guidance. Nonetheless, it is an interesting trend worth monitoring. If it were to continue (and thus wipe away the pulling-guidance skew), this would be a strong signal that the expected 44% decline in earnings for 2Q was too dire (recall the expectation for 2Q back on April 1 was a drop of 12%).

- Sporting goods trend continues

Here is a good chart from the WSJ. We believe this is one of the trends that might stick after the virus fades away. Obviously, there will not be percentage increases like this going forward. But the theme is solid, and it ties in directly to the population movement out of the urban areas. This is exactly why we started buying some of the outdoor leisure-good makers (despite missing the bottom and the bounce).

Percentage change in sporting goods spending vs. the same week a year earlier

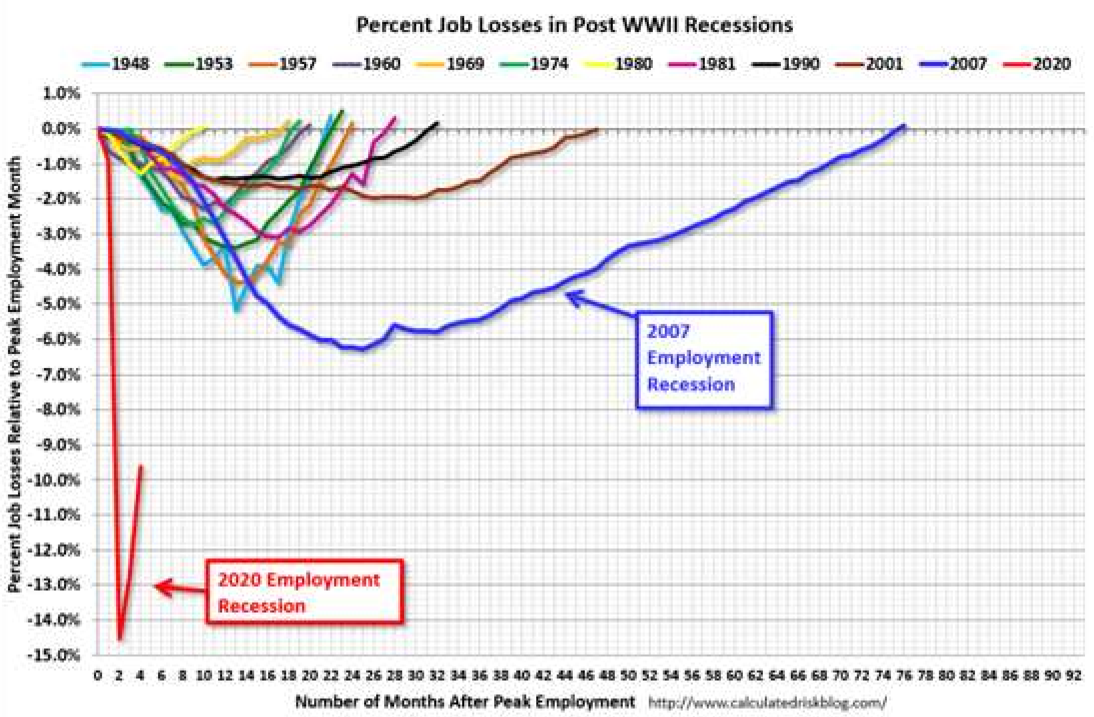
Note: "Early reopeners" includes states that, as of May 11, had no shelter-in-place order and allowed indoor dining (AL, AK, AR, FL, GA, IA, IN, KS, OK, MO, MS, MT, ND, NE, NV, SC, SD, TN, TX, UT, WY).
Source: Earnest Research

- Employment bounces back strongly, but beware of the data

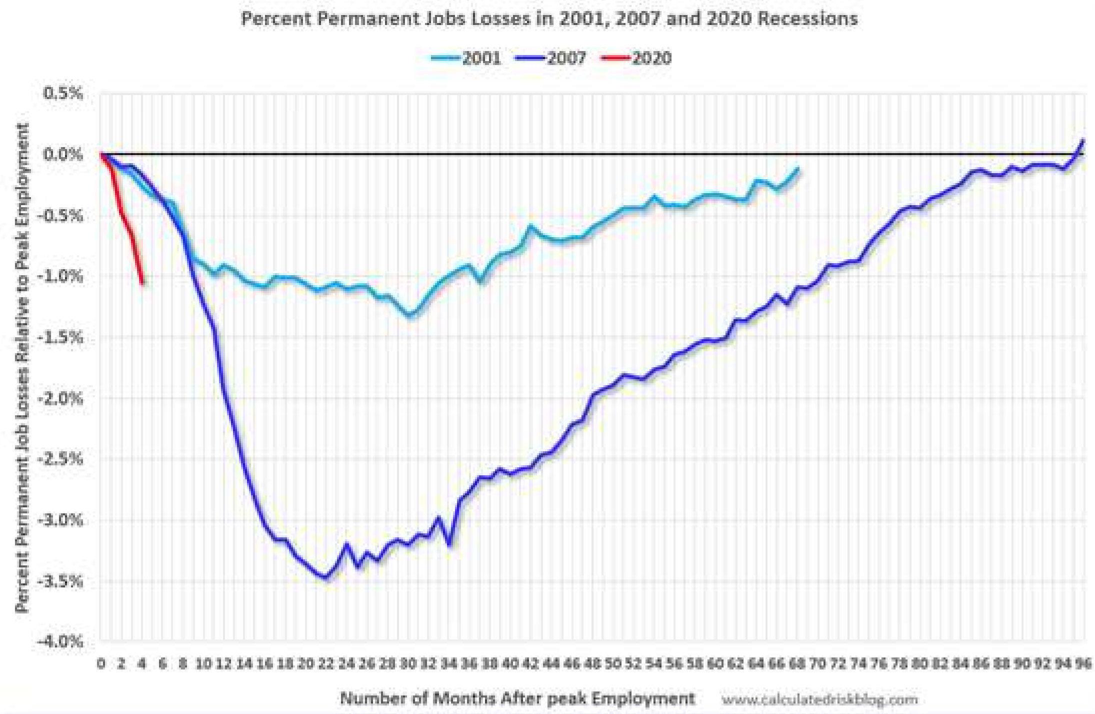
We had another banner Employment Report with a huge 4.8mm gain in jobs in June. The loose consensus was for a gain of 2.9mm. The Unemployment Rate fell to 11.1% from 13.3% and 12.4% expected. As is the new norm, the numbers are muddled. Temporary job losses fell dramatically (people went back to work). But permanent job losses, conversely, jumped. Another twist is that half of the new jobs are part-time workers. This ties into another increase in Jobless Claims last week (1.4mm) as part-time workers can still file for unemployment assistance (insurance). The JOLTS report (Job Openings and Labor Turnover Survey) showed a similar trajectory with a huge decrease in Separations (fell from 9.9mm to 4.1mm) with an accompanying increase in Hires from 4.1mm to 6.5mm. Unfortunately, this is May data…still positive obviously. But a relevant highlight is that of the 4.1mm Separations, 2.1mm of these were Quits. Some of these could be out of fear, and there is no way of knowing. But we suspect a good portion of these are legitimate in so far as they were looking/moving to better work (perhaps a waiter getting very few tips decided to join the ranks of Amazon, or something along these lines).

As we have noted, much of the confusion in the unemployment numbers stems from how workers are classified. As it turns out, it is not necessarily the fault of the out-of-work employee. Most firms are telling their workers they are being furloughed instead of outright dismissed. For small companies, this optimism has soured (more permanent losses). For large companies (with better access to capital and more flexibility to adjust business practices), the can is till being kicked down the road. Of the 87 S&P 500 companies that have adjusted workforce numbers, 65 have been "temporary" furloughs.

Bloomberg wrote a piece right along these lines. It showed the disastrous graph of jobs lost in this recession vs the previous 11 (and it is % losses). But this chart, like most, does not breakdown the losses into temporary or permanent losses.



But we know that many of these lost jobs are being classified as temporary. The better chart is one that shows already permanent job losses. As you can see, the speed of the losses is still remarkable. But the depth and duration are only a fraction of the last recession. While the optimists think that with a quick vaccine or therapy the world will go back to the way it was. The realists understand that many of these temporary lost jobs will, indeed, become permanently lost.



The two PMI surveys for Services showed the same rebound as the rest of the economic data. The Markit survey increased to 48 in June from 37.5 in May. The ISM surged to 57 from 45. This looks like a great number as it is back to pre-virus levels. But remember, this is a diffusion index which only measures the change on a rolling monthly basis.

- Quick Hits
  - Uber says its Eats division will be profitable on an adjusted EBITDA basis in two of its five largest markets. We might have missed a qualifier or two.
  - Uber is buying Postmates for $2.6b. Life-to-date, Postmates has raised and incinerated $900mm.
  - The Ayn Rand Institute asked for and received a PPP loan between $350k and $1mm.
  - Gold ETF's have had record inflows of $5.6b in 2020. This amount of physical gold can fit into about 14 gallons.
  - Some of the better performing dividend mutual funds have Microsoft and Apple as their top holdings (yields of 0.98% and 0.88% respectively). Caveat Emptor.
  - The Chinese government holds frozen pork reserves.
  - The bubonic plague still exists. It can be treated with a simple antibiotic.

*****Vox reported that "early research also suggests that people infected with the coronavirus experience lung damage and other long term complications…" How in the world do we know there are long-term complications? As we keep saying, let us stick to facts and numbers and leave the politicking to the twitterverse.

Trading: We sold our QQQ Calls after they blasted higher again. We also added to some of our more conservative stocks. This is a way of getting more equity exposure without adding too much risk. Obviously, this is not a no-lose situation. But these specific stocks had good news, so it seems their growth prospects are intact. We also added to some of our healthcare positions. Going back to QQQ, we still believe strongly in the leadership for the long term (Microsoft, Apple, Amazon, Google, Facebook, Nvidia, etc). But we are getting to extremes which might warrant some trimming. For what it is worth, Tesla, gulp, is now the 6th largest holding in the Nasdaq 100 (QQQ). So, we can happily say we have made good money off being long Tesla!!!!!!!!!!

TSLAQ: See the last sentence above! As for news, Tesla reported a drop in sales for 2Q, but the bulls raved about it being better than the dismal expectation. All the analysts are upgrading their price targets and basically jumping on the bandwagon. The skeptic in us thinks these banks are just trying to catch a piece of the investment banking business that is surely coming down the pipeline. Elon would be a fool if he did not sell enough equity at this insane valuation to pay off all his debt and fund the truckload of capex necessary to build all of his pipedreams. Do not forget, The Villain said the price was too high around $700. It is now double that.

Carlisle's Twitter Financial List

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