Weekly Update

14-July-2021
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- Market sits at highs as Big Tech routs everything else
- Earnings season has begun: strong results, bad reactions
- Employment improving albeit slowly
- Inflation is still a worry (but not really)
- Fed dissent grows louder, but monetary policy will remain easy
- Oil Volatility has picked up, and it might increase
- Chart Crime of the week
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	Last	5d %	YTD %	1yr %
SPX	4374	0.4%	17.2%	40.7%
QQQ	363.1	0.6%	16.0%	41.2%
US 10 YR	1.35%	1.31%	0.92%	0.63%
VIX	16.3%	16.2%	22.8%	27.8%
Oil	72.93	1.0%	50.7%	81.5%

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

With the headline equity market indices sitting near all-time highs, it would be easy to think everything is rosy with the economy. Well, a simple look under the hood tells us a different story. 10-year interest rates continue to plunge (below 1.3% at one point). This is a message from the bizarro-Bond Vigilantes who are telling the market that the economy is not in good shape. Along these lines, the more economically sensitive stocks, Small-Caps, are underperforming with the Reopening names really struggling. Of course, Big Tech thrives off low interest rates and a status-quo environment. And Big Tech is what drives the headline equity indices! This move is even more impressive given the amped up regulatory pressure on Big Tech. But so far, the arguments against the market titans have only been conjured up as ideological rants by economically illiterate congressmen like Maxine Waters. Moreover, with Nancy Pelosi adding long Amazon Calls to her portfolio, we doubt any serious regulation is coming down the pipeline (not to mention, lo and behold, the government is putting the cloud computing contract that Microsoft had won back up for bid thanks to Amazon's lobbying). To the flip side of Growth is the poor performance of Value lately. This ties right into the reopening theme…or the lack of it. Reflation has stalled (which drives much of the Value trade). Sitting in the middle of the Value vs Growth debate is the High Growth segment. These companies benefit from the long runway supplied by ultra-low interest rates. But weak economic growth overrides or at least blunts this tail wind. That is, the stretched valuations that have been ignored are no longer being ignored.

The inflation narrative is still running hot. We still think it is mostly transitory given the dispersion of price increases is tightly grouped around the post-pandemic shocks. And we still maintain that labor pressures will ease in the fall (although to be fair, the easing has been very subtle so far). But the rate of change of these isolated points of inflation is back to increasing not decreasing. So, the jury is still out.

While we have continued to harp on the nonworkers-getting-off-the-couch theme when government stimmies end (Sept 6 for the Dem states that have not opted out) as well as the impending end to the eviction moratorium (July 31). But another financial cliff is worth mentioning. Student loan payments have been frozen since March of 2020. The immediate thaw will hit on September 30. Obviously, student loan forgiveness is a real threat (errrr, possibility). But unpaid balances on the $1.7t in student debt outstanding is a heavy burden (underwater basket weaving is more legitimate than most college degrees nowadays).

- Earnings season has begun: strong results, bad reactions

Financial stocks have kicked off the earnings season. Cutting to the chase, we should always buy Financials ahead of their of earnings and subsequently sell them right before the first releases. These stocks routinely beat expectations. But, alas, apparently, they rally too much into earnings and never beat expectations by enough. Moreover, the market tends to focus on the weak areas. This week, the investment banking revenues were much better then expected. The reversal of loan loss provisions on the banking side was expected (but still positive). But slow growth in loan originations juxtaposed with high growth in deposits is a bad mix. Throw in a flattening yield curve (having to pay more for these increasing deposits relative to lower interest rates on their loans), and the short-termers headed for the exits.

- Employment improving albeit slowly

The Employment Report seemingly improved on the headline as the number of new jobs in June outpaced May and expectations (June: 850k May: 583k Exp: 700k). Unfortunately, Government jobs accounted for a chunk of the surprise (Private Payrolls increased 662k vs 600k expected). The Unemployment Rate ticked higher to 5.9% while the Labor Participation Rate remained the same at 61.6%. Average Hourly Earnings increased at a 3.6% annual pace. Separately, Jobless Claims ticked lower to 364k vs 415k last week. We still think the employment situation will continue to improve. Although, we must admit, the ISM and PMI surveys are still showing companies experiencing trouble in finding workers. Perhaps the folks on the government dole are riding out the summer until they get back to work? Anecdotally, we saw "Now Hiring" signs throughout the nine states we traversed.

- Inflation is still a worry (but not really)

The Consumer Price Index (CPI) continued to surge higher with the June annualized rate hitting 5.4% (up from 5.0% in May, 4.2% in April, and 2.6% in March). Ex-Food & Energy price increases also remain elevated at 4.5% vs 3.8% in May. Last month, we noted that the rate-of-change increases in inflation had started to slow. That is not the case this month. To the contrary, the Atlanta Fed's Business Inflation Expectations declined in June to 2.8% from 3.0% in May. Further to the expectation theme:

- Fed dissent grows louder, but monetary policy will remain easy

The tally of Fed members that are in favor of starting to taper bond purchases "sooner rather than later" has reached four. Patrick Harker of Philadelphia is the latest to join the minority refrain. Eric Rosengren of Boston thinks tapering could start this year with a rate hike next year. Robert Kaplan of Dallas wants to "take our foot gently off the accelerator" because the economy is suffering from a supply problem not a demand one. And James Bullard of St. Louis let it be known following the last Fed meeting that there is "upside risk" to inflation and that the Fed must be ready to act.

Along these lines, the Fed's Beige Book (a gathering of date two weeks before the next FOMC meeting) seems to indicate that inflationary pressures will remain for the short-term but will still be transitory.

None of this changes our view that the Fed will remain accommodative. Powell is in charge, and he is squarely in the dovish camp despite acknowledging the future need to taper bond purchases. On top of their inflation view (it being transitory hence no imminent tightening of monetary policy), we think they are overestimating the stand-alone strength of the economy. By stand-alone, we mean without government stimulus. We think this will become clearer. With this new economic weakness should come deflationary pressures. As an aside, we wish the Fed had hiked ages ago. This gradual peeling and reapplying of the band aid will likely end badly.

- Oil Volatility has picked up, and it might increase

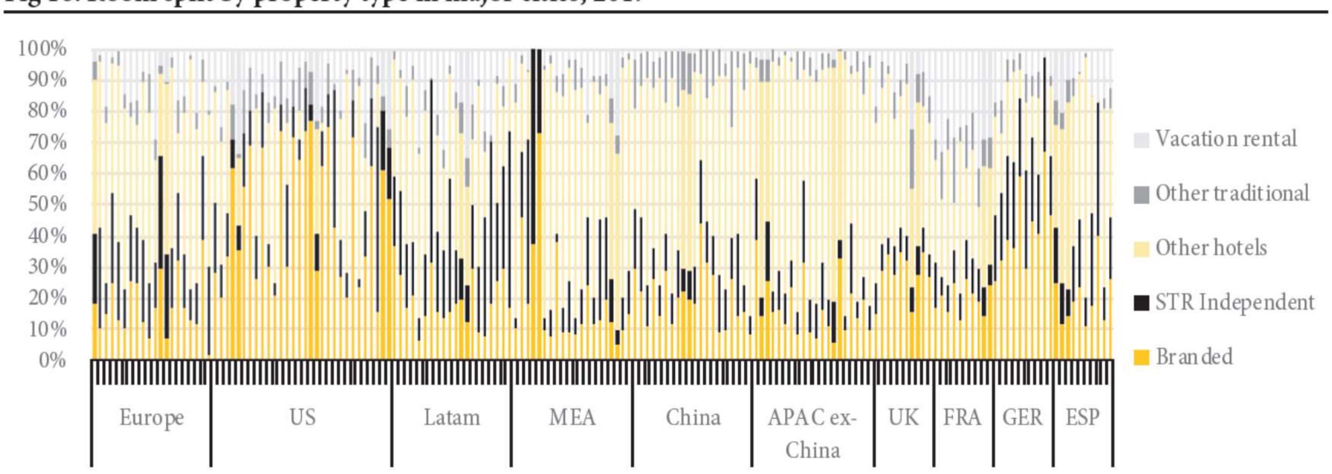
Crude Oil volatility returned as the OPEC+ meeting did not conclude as expected. Reports were that OPEC and Russia would show more restraint in terms of hiking production: the band of rogue nations would only reduce its cuts (increasing) by 2mm barrels per day spread out between August and December (about 400k per month). But Abu Dhabi (actually United Arab Emirates, Abu Dhabi is the capital of the UAE and in control of its energy assets) threw a monkey wrench into the cautious plans. It wants to increase its own production by more than all the other countries combined. There is some speculation that the UAE might leave OPEC over this disagreement. Of course, the rift between Saudi Arabia and the UAE has been growing recently as UAE wants more of a leadership role (instead of always playing second fiddle to the Saudis). The market somehow took this as positive for oil prices. But when rational minds prevailed, oil started retreating (a breakdown of OPEC+ not to mention OPEC could cause an all-out oil price war akin to what we saw in April of 2020 when WTI spot prices went negative). Not so coincidentally, there were reports that US shale players continue to keep spending in check fearful of a supply glut. Conversely, near-term hedging by oil companies has dropped dramatically. It appears they are trying to game the curve around the OPEC+ decision (not selling selling via short-term hedges but they expect weakness further out in time). It is also worth noting that Chinese oil imports fell 3% in 1H2021 vs 2020. This was the first decline since 2013.

Strangely, actual oil Volatility as measured by the OVX has been sitting in a pretty tight range. We think this is a function of positioning as macro traders have increased their long oil positions substantially. The point being is that realized Vol will pick up as soon as the trend-following macro guys start to waver.

- Chart Crime of the week

Our head hurts trying to even figure this one out:

Fig 16: Room split by property type in major cities, 2017



Source: Redburn, STR Global, AllTheRooms.com

And we will throw in a bonus "Newspaper Headline" of the week:

Latest on US economy

EU jobless numbers drop by most since pandemic hit

Economists can't predict the future — policy should reflect that

FT-IGM US Macroeconomists Survey US economy + Add to myFT

Economists predict at least two US interest rate rises by end of 2023

Inaugural FT-IGM survey of academics points to messaging challenge for Federal Reserve

- Quick Hits
    - D'Eriq King, the quarterback for the Miami Hurricane, is one of the first college athletes to monetize his NIL (name, image, likeness) with a $20k contract with College Hunks Hauling Junk
    - Antwan Owens, a defensive end at Jackson State, signed a deal with 3 Kings Grooming.
    - 200 Americans die every year in collisions with animals. (Personal observation: roadkill is up massively in 2021).
    - Some spiders can propel themselves high enough into the air to reach a jet stream and thus "fly" for 25 days.
    - Graduate School debt accounts for 40% of all student debt in the US.
    - Graduate students account for 20% of student borrowers.
    - Apple and Amazon gained more in six recent sessions that the total market cap of 479 members of the S&P 500.
    - Twitter has country specific "grievance officers."
    - Binance in the UK is not processing cash-out requests (crypto for GBP$). Binance is the largest crypto trading platform.
    - Crypto trading shrunk 40% in June vs May.
    - The buyer of Reebok from Adidas has backed out of the deal because Adidas demanded that the new buyer operate Reebok as a standalone business.
    - South Africa's unemployment rate is 33%.
    - John Cougar Mellencamp gets the most radio time in America.
    - Aha's "Take on Me" is the most popular one-hit wonder of all time

Trading: As the narratives continue to swirl and rotate, we are holding steady. We still have our long exposure to small-caps, Value, commodities, and the Reopening theme (these have given back some of their relative performance). But we are balanced with plenty of Big Tech (making new highs). We have started to add more to our Reopening themes. We think there might be some virus-fear creeping back into the market. We think this is a mistake to trade this (believing it). So, we are trading against it. At the same time, we might lighten up some of our long Big Tech. While it is seemingly in a relative sweet spot, its collective valuation is rich. Of course, that does not mean all of these names should be sold. We will likely finetune some of our exposure here to capture any dichotomies. We have also increased our event-driven allocation. These trades theoretically do not rely on the direction of the market. This is certainly not always the case. But adverse movements are usually opportunities.

TSLAQ: Electrek, the mouthpiece for Musk masquerading as journalism (the owner admits to being long Tesla shares), is now writing with a straight face that some of the Tesla car fires might be arson by short sellers. Elsewhere, Musk finds himself back in court trying to defend the Solar City acquisition. While maintaining that he does not control the board and that he never forced Tesla to buy his other company, Solar City, Musk submitted that he hates being the CEO of Tesla but Tesla would "die" without him.

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