Chalk Creek Partners LLC

Registered Investment Advisor

Weekly Update 22-July-2020

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- Market rally continues, and it is not all Big Tech
- Unemployment Benefits are not trending as well as thought
- Retail Sales and Housing continue their bounces
- The ECB overshadowed the Fed this week

	Last	6d %	YTD %	1yr %
SPX	3227	1.5%	1.4%	9.8%
QQQ	264.9	1.5%	24.6%	37.6%
US 10 YR	0.60%	0.63%	1.88%	2.08%
VIX	24.3%	27.9%	23.2%	12.6%
Oil	41.92	2.3%	-31.4%	-25.5%

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

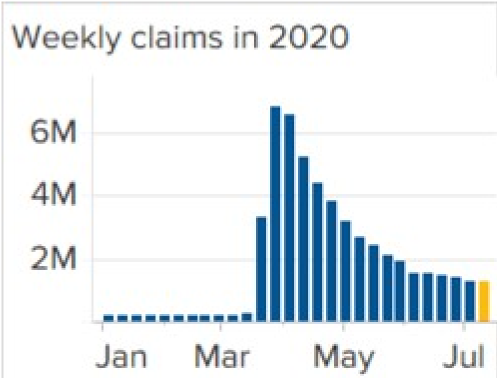
The market continued its epic rally. Just check out the year-to-date and 1-year performances for the indices in the above table! The drivers of the market continue to be hopes for a vaccine, more fiscal stimulus, and a natural recovery in the economy. We still think a vaccine is fool's gold in theory (at best it will be like the hit or miss seasonal flu vaccine). But as we have been saying, just easing the fear of the people might be more important than the actual medicinal effects. Along these lines, after Trump tweeted a picture of himself wearing a mask, leisure stocks had a big rally. While the unemployment numbers are still startling, Retail Sales and Housing continue their robust recoveries. The European Union added to the helicopter money with another stimulus package. If the US congress can come to terms on another round of stimulus, the party might last longer.

The leadership in the market does seem to be shifting. Or rather, it was not a one trick pony with only Big Tech leading the way. Utilities were the best performers by far with a gain over 4%. Materials and Healthcare were the next best performers.

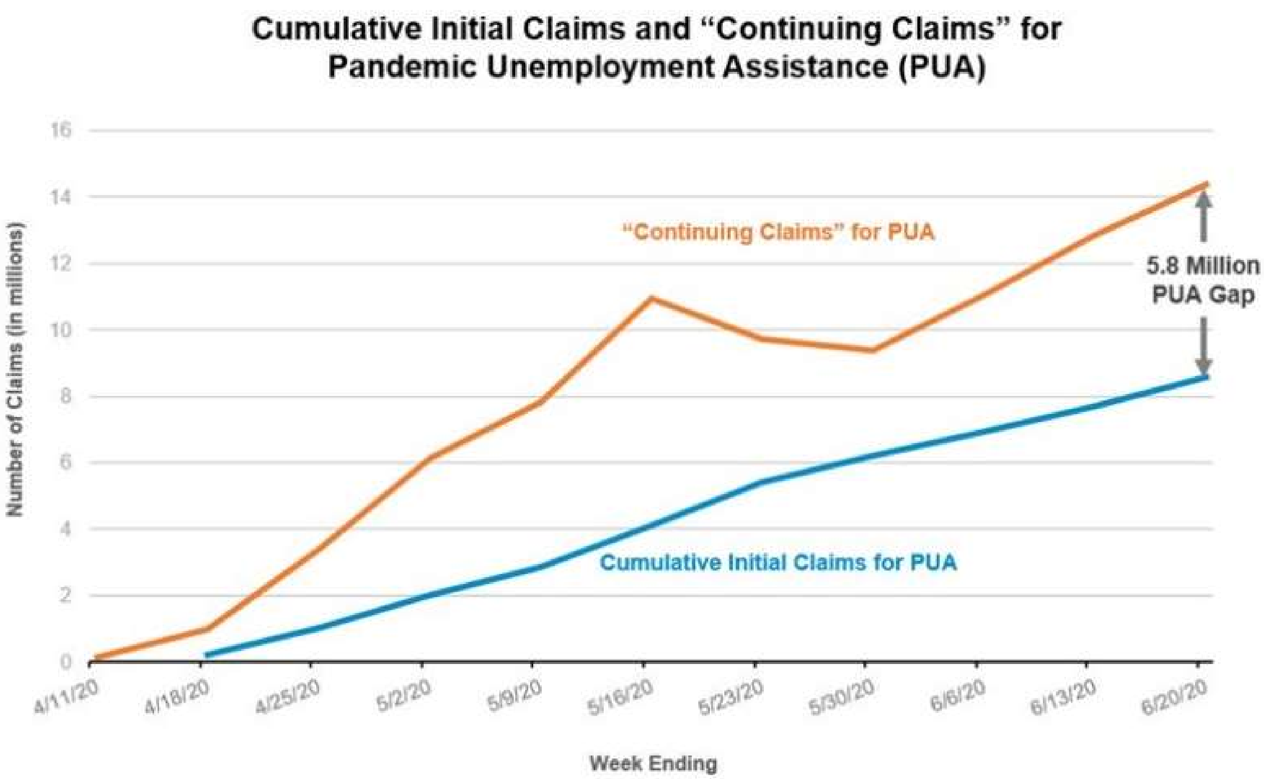
This week's virus stat is the deaths per 1mm of population. New Jersey and New York still sit atop with 1,777 and 1,677 per capita deaths. The much-maligned California, Texas, Florida, and Arizona: 203, 156, 249, and 409.

- Unemployment Benefits are not trending as well as thought

Jobless Claims tallied over 1mm for the 17th straight week. On the positive side, the 1.3mm new claims was the 15th week during which Claims fell from the preceding week. But the rate of decline has slowed.

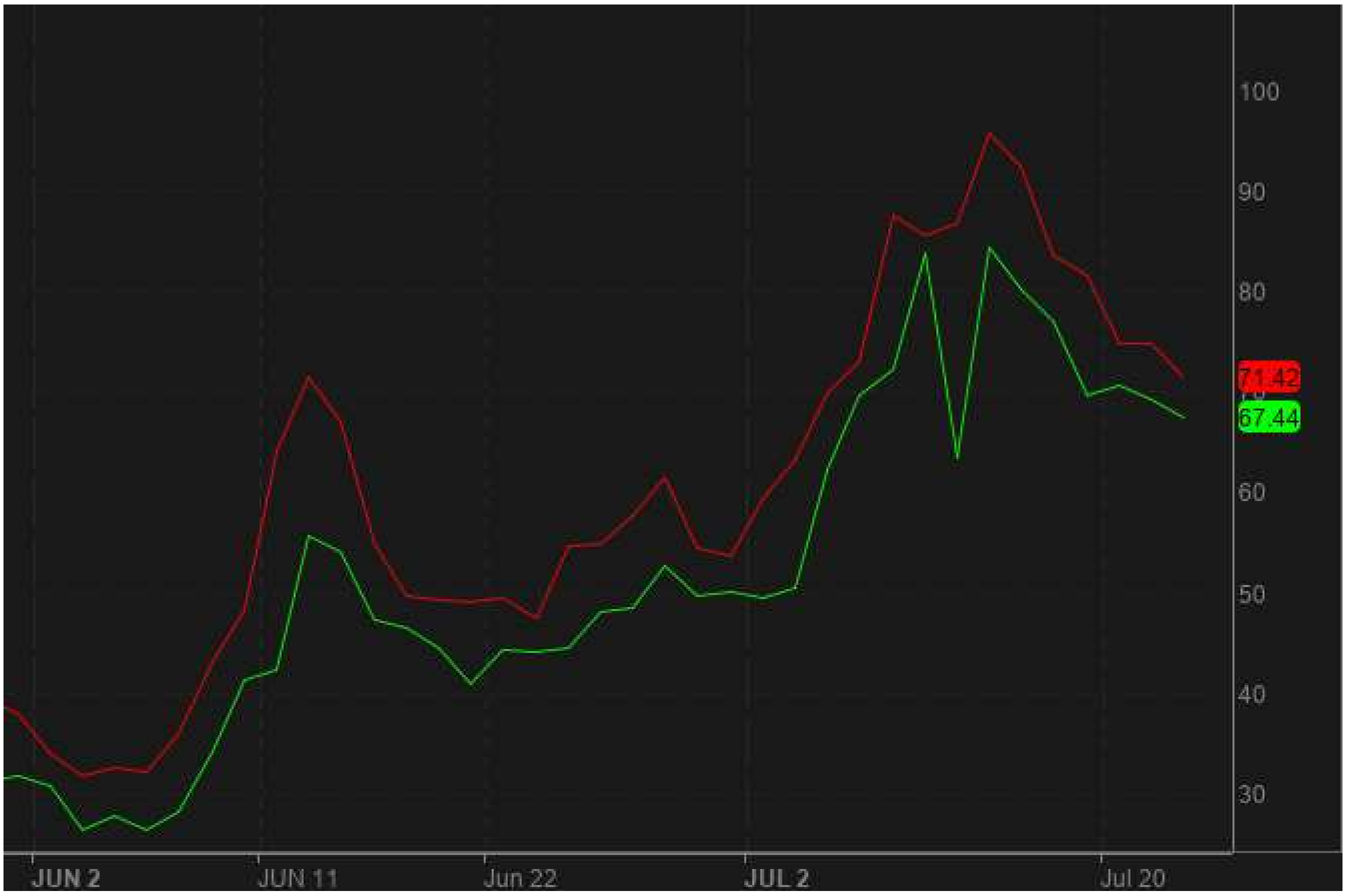


Continuing Claims also dropped again. 17.3mm is the number collecting state unemployment benefits. But the federal Pandemic Unemployment Assistance claims jumped again. The total is now 14.4mm. Of course, we cannot forget that this number includes multiple claims by the same individuals because they are filing for missed weeks (backdating). Here is another version of the chart showing the Claims Gap for PUA claims. Even if the Continuing Claims are inflated (orange line), the trend of the New Claims (blue line) is still worrisome.

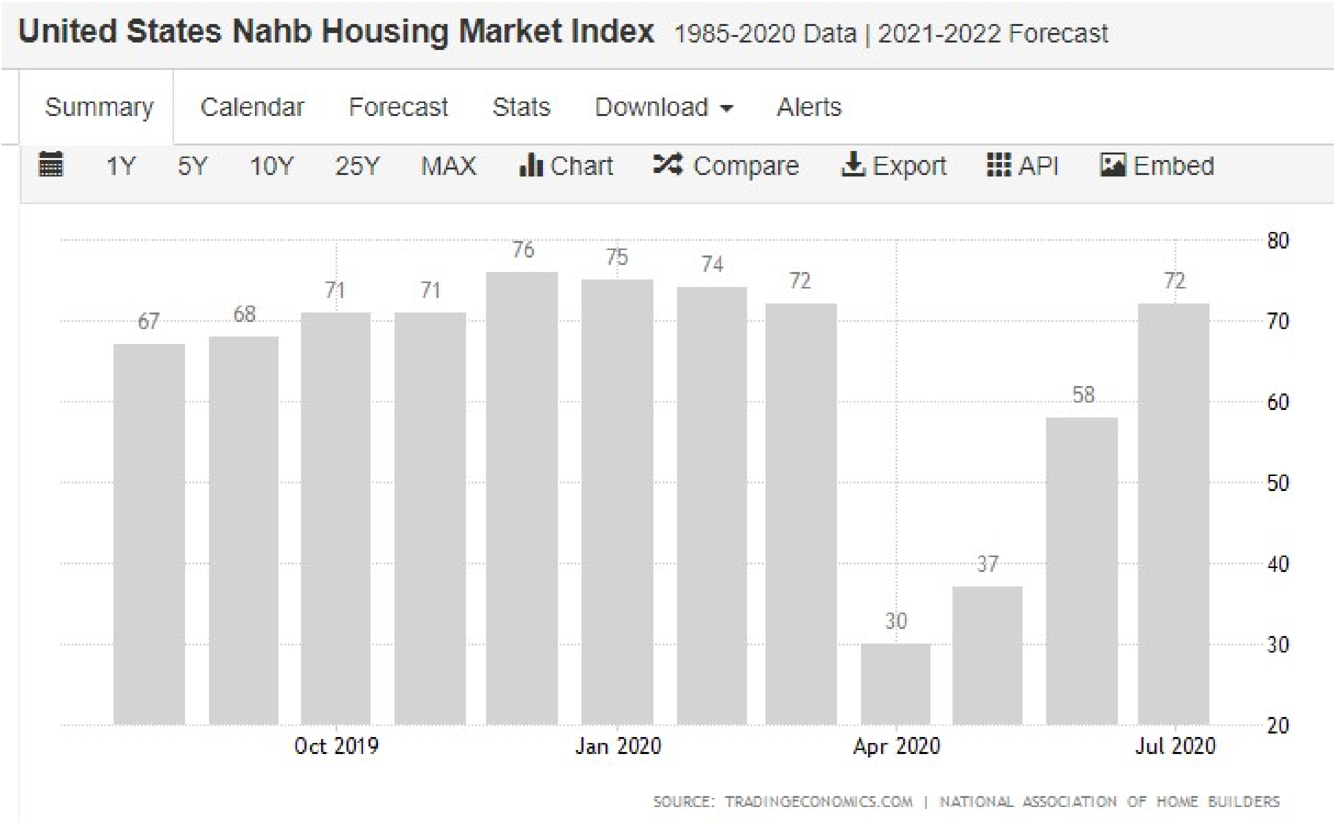


- Retail Sales and Housing continued their bounces

Retail Sales continued their comeback with June increasing 7.5% vs May. May's increase vs April was revised up to 18.2% from 17.7%. Even though the Fed just said auto sales have rebounded well, the majority of the outsized strength (7.5% vs 5% expected) came in "Sales less Autos." The specific categories that performed the best are no surprise: building materials and garden (recall last week's noting of lumber prices rallying 60% in 2Q), grocery stores, sporting goods (as we keep highlighting), and nonstore retailers (aka e-commerce). Unsurprisingly, e-commerce sales led the charge with a 23.5% gain (annoyingly, this is a year/year rate (June 2020 vs June 2019) unlike the headline which is month/month (June 2020 vs May 2020)). The weakest segments were electronics, health and personal care, large department stores, and home furnishing. However, along with the reversal in the easing of government mandates (more tight policies), the weekly Retails Sales figures by Redbook show declines. Merrill echoes this by saying its channel checks show Retail Sales started to slow near the end of June. This will obviously be key to watch. This might be what has caused Amazon to wobble a bit lately (or at least become much more volatile). Here is a chart showing Amazon's Implied Volatility Rank (IVR). It simply shows that Amazon's Volatility (as measure by its options) in early June was in the bottom 30% of readings over the last year, and then it climbed higher over the next six weeks.



The housing market continues to shine. The Housing Market Index, a survey of home builders and perspective buyers with their views of the market, jumped back to pre-virus levels. The single-family homes sub-index showed the most optimism.

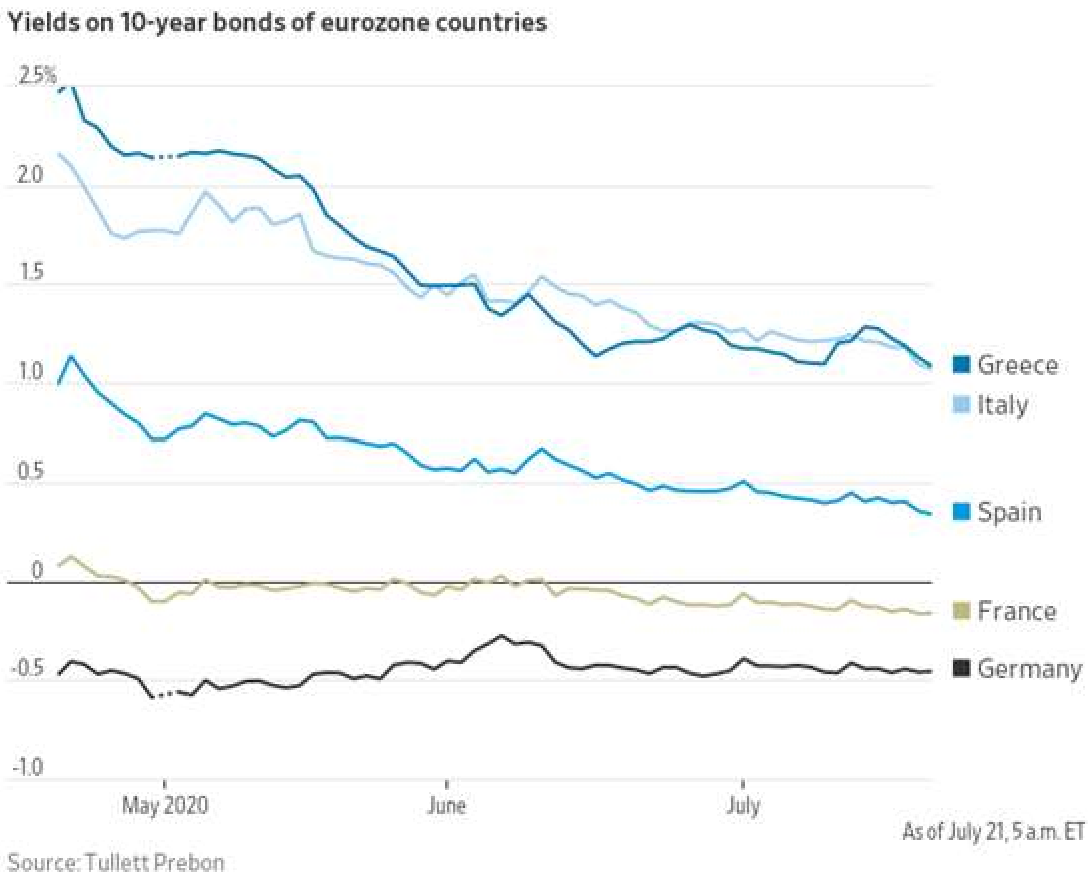


Housing Starts also jumped nicely in June vs May. The headline number was 1,186,000 starts with a 17.3% increase vs May (recall this is one of those quirky stats that uses annualized numbers). Both single family and multifamily homes (five or more apartment units) increased sharply. Building Permits, however, only increased 2% against May compared to May's 14% jump vs April. Existing Home Sales surged almost 21% in June vs May.

- The ECB overshadowed the Fed this week

The European Union passed its "permanent" stimulus package of E$750b ($855mm). After some wrangling by the more responsible nations (funnily called the Frugal Four), E$390b will be grants with the rest being loans. Importantly, the group of nations will jointly underwrite bond issuance to pay for the "Reform and Recovery" plan. Despite the obvious increasing of its money supply, this is seen as a positive for the Euro currency because of the collective nature of it. This should add to the recent USD weakness. We like US multinationals with foreign currency exposures because of this.

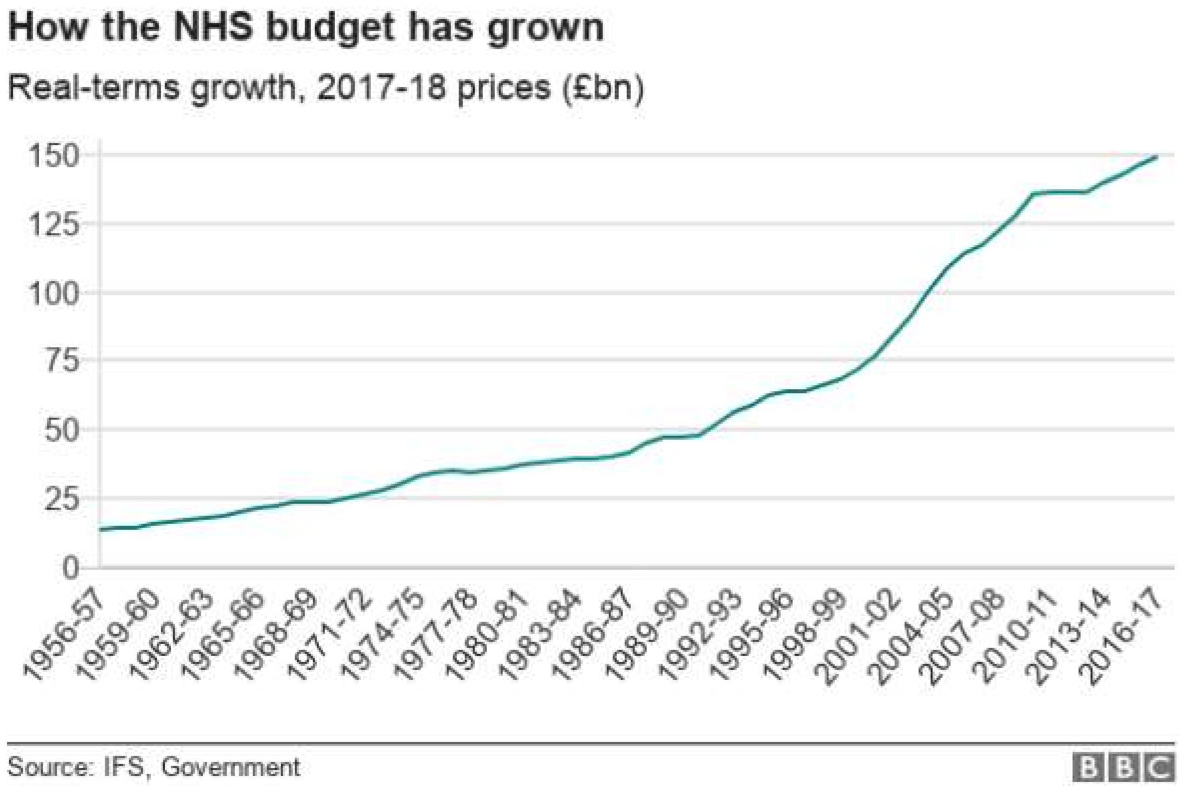
For what it is worth, this E$750n is on top of an already-passed E$540b short-term fiscal stimulus. The EU also passed a seven-year budget totaling E$1.074t. And let us not forget the Pandemic Emergency Purchase Program which allows for the ECB to buy E$1.35t in government bonds. So, while we think the USD should weaken some, it is not as though the Europeans are some bastion of government spending austerity. Nonetheless, the ECB has done a good job of compressing the spreads of the member states's (more like states now than nations) government bond yields.



The Fed balance sheet broke its four-week shrinkage streak as it increased by $38b last week to sit back above the $7t level. The swap and repo facilities continuing to decrease in size (these are the overnight, stop-gap liquidity measures). The emergency lending facilities are still barely being used. The vaunted Main Street Lending Facility made a whopping $12mm in loans. Alas, the balance sheet got larger due to classic Quantitative Easing…the Fed was buying treasuries and mortgage backed securities.

The Senate Banking Committee voted to approve the two nominees to the Federal Reserve Board of Governors. Judy Shelton is considered the controversial nominee since she was an advisor to Trump in 2016 (and she is a big gold advocate). But we do not see anything nefarious in this appointment or her views. Moreover, with only 19 people (12 regional Fed presidents and 7 Governors) debating and contributing to monetary policy, some outside thinking should be welcome.

- Quick Hits
    - Colleges received $14b in Cares Act money. They claim the costs to reopen will be $74b.
    - Johnnie Walker is going to come in paper bottles in 2021 (like milk cartons).
    - Jeff Bezos made $13b on Monday (these stats are always stilly, but this one stood out).
    - The 100yr old Brit that walked in his backyard raising $40mm for the NHS was finally knighted by Queen Elizabeth.
    - John Cleese and David Bowie both turned down knighthood.
    - The NHS, the socialist medical system in the United Kingdom, spends about $190b a year. Remember, childbirth with a doctor is not covered by the NHS. But if the mom dies, it is free.



Trading: We added some more of our conservative equity positions after last week's addition of Put protection on Big Tech. These names are reporting strong earnings and seem to be the recipients of an early rotation. While we might not see a full-fledged rotation given these companies are not cheap on a valuation basis, it is likely that they will hold up better if Big Tech starts to fade. Using our traditional barbell strategy, we also added small amounts to our Recovery bets (airlines, energy, and high-priced leisure items).

TSLAQ: Tesla reported a profit for the 2Q. Of course, the bulk of the profits came in the form of regulatory credits. Recall, other auto companies are paying Tesla because various governments are forcing car makers to make Electric Vehicles (EVs). Automotive Margins declined. Cash Flow surprised on the upside, but then again, the company did not disclose if it had reduced capex which will obviously have to be reversed if it plans on building more factories. Revenues declined. But hey, this is a growth story! Looking ahead, we will look to re-enter a short position via Puts. It is likely to see some more momentum because it might enter the S&P 500 index. But index inclusion trades are usually sucker plays. That is, funds have obviously been buying in anticipation of this – buy the rumor and sell the news. Of course, this is a momentum name, so we need to see things stall before we act. If nothing else, puts could just neutralize our passive long in Tesla since it has been a growing weight in our long Nasdaq exposure.

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