Weekly Update

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- Are we growing or not?
- Volatility is here to stay
- Positioning is still stretched
- Buybacks are coming back slowly
- GDP growth was likely pushed back from 3Q to 4Q
- PMI Surveys show continued strength in Manu with a global divergence in Services
- China is slowing, even the Communists admit it!
- OPEC is not caving, nor is Biden (quizzically)
- The UK's energy crisis is of their own making
- Chart Crime of the week

	Last	5d %	YTD %	1yr %
SPX	4400	2.1%	18.3%	32.8%
QQQ	363.0	1.4%	16.1%	32.6%
US 10 YR	1.58%	1.51%	0.92%	0.80%
USD/DXY	94.2	94.3	89.9	93.6
VIX	19.5%	22.6%	22.8%	26.4%
Oil	78.85	5.1%	59.6%	96.0%

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

The uncertainty around the economic outlook continues to be the central battleground in the markets. There is little doubt that stagflation was the overriding economic condition during the 3Q. Growth kept slowing while inflation kept increasing (be it transitory or not is irrelevant). But with the umpteenth wave of the virus-fear having seemingly faded (again), the economy could be ripe for another Reopening (and this is our view). With the Fed intent on simply tapering its bond purchases and not hiking interest rates any time soon (maybe a year from now? who knows), rising interest rates on the long end signal that the economy is growing. During Stagflation, we get a flattening of the yield curve. As we discussed last week, the yield curve has steepened. Of course, it is not this simple.

The body blows to the market psyche keep coming like Soda Popinski uncorking on Little Mac. The global energy crisis is intensifying despite plenty of signals that things should be cooling. China is in the background now, but another property developer missed a USD debt payment (Fantasia Holdings…the bond holders no longer find this name so funny). The debt-ceiling drama might be concluding…at least for a few more weeks.

This helped the market rally today. But we will likely play this all over again come the next deadline. Even with a Reopening, we could still be at peak growth for the market as a whole. Virus vaccines may not be all they are cracked up to be (we do not want to go down this political rabbit hole here). Valuations are still nuts. Biden seems to be picking up the China trade war right where Trump left off. Despite our near-term mild bullishness, we will have a quick trigger finger in case things start to fade again.

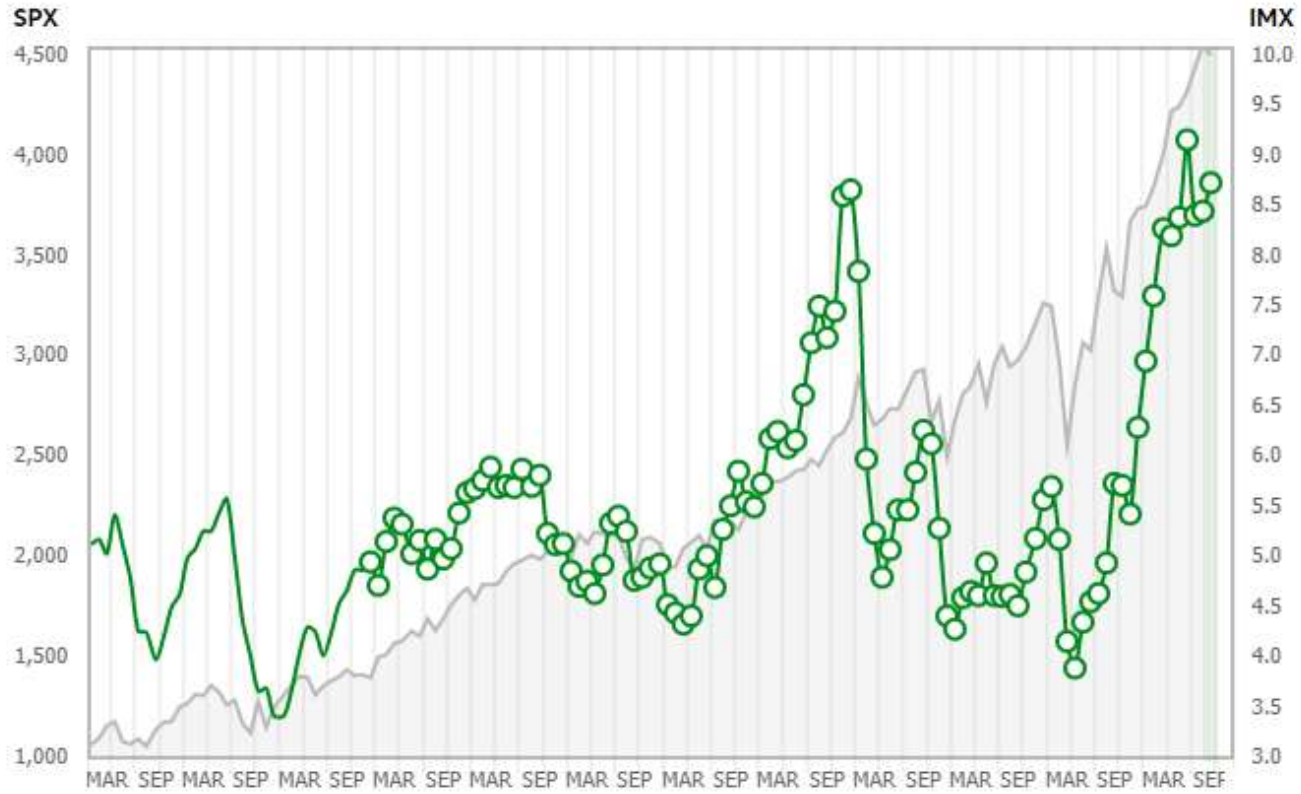
Another wildcard that continues to bewilder us is the labor situation. The number of Job Openings remains at an all-time high. Johnny Paycheck is alive and well even without the federal pandemic unemployment benefits. We are watching the Savings Rate waiting for it to fall further. How can 8-10mm people simply not be returning to the workforce? Maybe they are the Bitcoin genius we read about on Twitter. But probably not. Until this gets resolved, labor costs are going to continue to increase.

- Volatility is here to stay

Here is a snapshot of the S&P 500's intraday trading over the last five days before today's rally. For a dead flat market, the moves were violent. The shaded areas are the after-hours session. Vol traders are probably able to lick it up. And perhaps they are rocking and rolling all night and partying every day. They were made for loving this trading environment.

- Positioning is still stretched

We like to talk about the positioning in the market. We stumbled across a new indicator from TD Ameritrade that gives a reading on the positioning of the retail investor (TD has over 11mm retail accounts, this will quadruple once TD completes its integration with Schwab). This IMX dates to 2012 (the chart below was retroactively fitted a few years before that). Our take on it is sharp pivot points probably have some value. And right now, positioning is still very bullish despite the blip lower in 3Q.

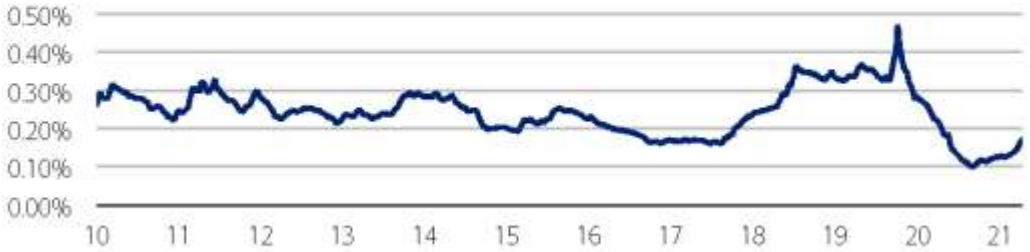


Merrill's data shows that their clients sold the bounce last week. Energy is still the sector attracting the most attention. Despite the overall net selling, investors were net buyers of small-caps and mid-caps while selling the large/mega-caps. Overall, they still have their highest allocations to equities ever.

- Buybacks are coming back slowly

There have been lots of headlines about corporate buybacks picking up steam. We have even noted it recently. But this chart puts it in better perspective. There is more to come.

Exhibit 3: Buybacks picking up, but below "normal" (pre-COVID) trends
Rolling 52-week BofA corporate client buybacks as a % of S&P 500 market cap, 2010-present



Source: BofA Securities, Bloomberg

BofA GLOBAL RESEARCH

- GDP growth was likely pushed back from 3Q to 4Q

The backward-looking GDP for Q2 was revised a touch higher to 6.7% growth from 6.6%. Looking ahead, 3Q GDP is looking to grow only about 3.5% (actually some professional guessers are as low as 1.5%). As recently as mid-July, the expectation was for 8% growth. On the positive side, much of the missing demand in 3Q has likely just been shifted out in time because of the virus-fear (delta variant). The question remains: Is the economy going to have another Reopening? Or has the delta-fear put an end to the growth phase we have enjoyed since the original virus-fear last March? We think we have one more burst of spending.

- PMI Surveys show continued strength in Manu with a global divergence in Services

PMI Manufacturing for September remains elevated despite a marginal slipping. Services are still hovering near their pandemic 16-month lows. ISM Manufacturing climbed more than a point to 61. More importantly, the trend seems to be improving. For Services, the increase was more subtle. But the overall level is still robust (62) just shy of its all-time high (63.5). The broad takeaway here is that the rest of the world seems to be catching up to the US's Reopening (recall the ISM focuses on large-caps and global companies). Obviously, the disjointed waves of the virus-fear account for much of the variance. And it is important to remember that these are diffusion indices. Just because one shows a strong reading does not mean it is a strong business opinion outright. It is explicitly a rate of change indicator (which is great, it just needs to be framed appropriately). We suspect (and are betting on) the US (and thus the Markit PMI reading) will start to outperform again now that the delta virus-fear is starting to subside.

- Looking ahead to Employment

Friday's Employment Report is expected to show a gain of 568k private jobs if we follow the guess by ADP. This report is supposed to include the first wave of the blue states relinquishing the federal teet. We think the elevated Savings rate (elevated but dropping) is still keeping the Family Guy from getting off the couch.

- Inflation remains high, will it last?

Inflation for August as measured by the Personal Consumption Expenditures (PCE) continues to run hot at 4.3% on a year/year basis (3.6% on the Core ex-Food & Energy). And the rate of change has leveled off (+0.4% and 0.3% respectively). Inflation Bears (it is transitory) will say flat is still a slowing. But the Bulls can easily point to the outright levels. We are still in the middle. We thought it would be transitory except for the virus-related supply chain problems. But our giant caveat was the self-fulling nature of inflation. The longer it persists, the stickier it becomes.*

The 5-year Breakeven Inflation Rate still sits right at 2.57% (this is a market interpretation of what inflation will be on average over the next five years). The 10-year expectation is slightly lower at 2.43%.

- Other Econ data seems average

Jobless Claims moved higher for the third week in a row until today's drop.

Construction Spending in August was about the same as July.

Consumer Sentiment in September ticked higher.

Factory Orders in August increased 1.2% vs July. This is about the long-run average. We would have thought it would be higher given the strength in Manufacturing. Perhaps the supply chain issues restrain the otherwise strong demand. We will try to figure this out.

- China is slowing, even the Communists admit it!

China's Manufacturing PMI for September fell below the 50 breakeven level. This is the first negative reading since February 2020. Somewhat oddly, Services have rebounded sharply. This data lines up with our observation from last week – that China is the most tied to global GDP and global growth suffered under Stagflation in 3Q. Local Services likely picked up as China is a on different rolling Covid timeline.

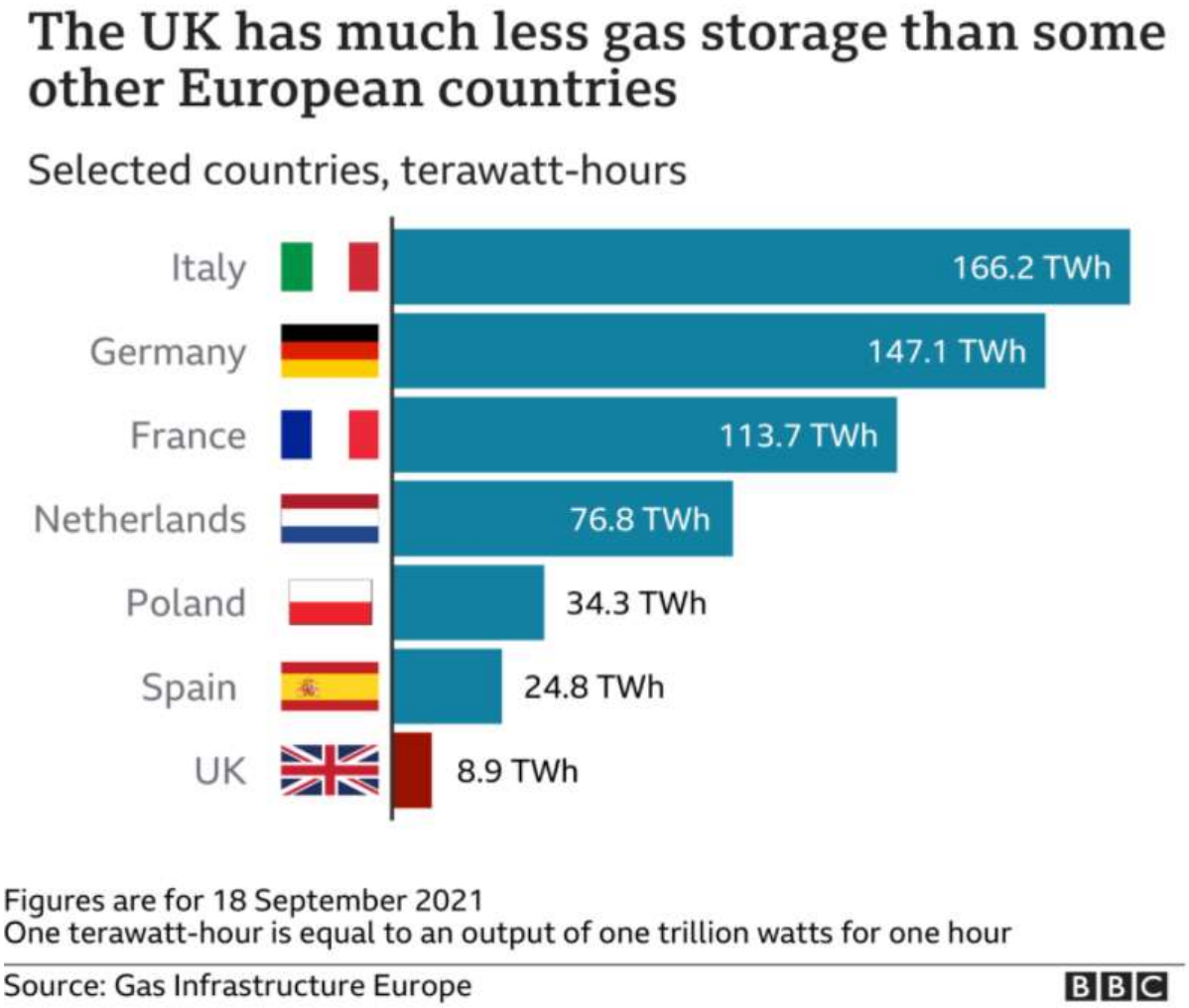
The Chinese Communists are showing their economic bonafides with respect to their energy crisis. On one hand, they have forced a reduction in coal usage for presumably green ambitions. But this has been hurting the economy. Banks are now being told to prioritize loans to coal companies.

- OPEC is not caving, nor is Biden (quizzically)

OPEC+ is going to stick to its modest pace of increasing supply by only 400k barrels per day in November. There had been some chatter that the group would boost supply next month by double the agreed upon amount (400k a month until April). Oil prices finally started to cool off after rumors swirled that the US government would release/sell oil from the Strategic Petroleum Reserve (SPR). The government denied this…and oil shot back up. We still like oil/energy.

- The UK's energy crisis is of their own making

The UK imports over half of its natural gas, and over half of this is from Norway (the US accounts for about 12% with Qatar at about 20%). But the real reason for its energy crisis right now is that it has no storage. Its "just in time" system was not very well thought out. (We wish this chart was adjusted for population. But since the UK is the continent's third most populous country behind Russia and Germany, we will allow it.)



- Chart Crime of the week

South Africa (Eskom) is the world largest sulfur dioxide emitter. This chart tells us how to stop this pollution. Who knew stopping "climate change" was so easy?

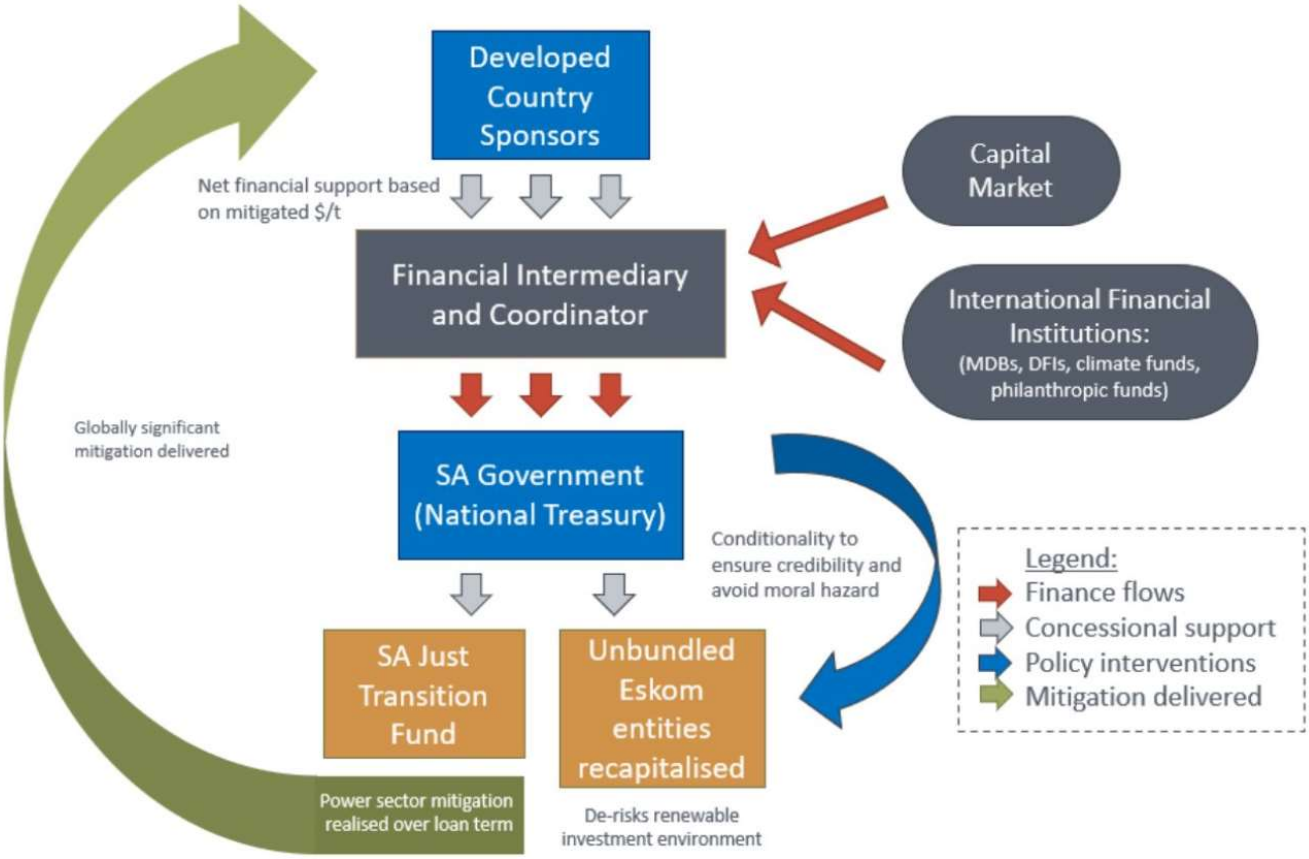


Figure 6: JTT Institutional structure and flow of funds

- Quick Hits
  - When the stock of the South Sea Company plunged in 1720, one British legislator proposed putting each company director in a sack. The sack would also have a monkey and a snake…and it would be thrown into the river.
  - Macy's owns the property of its flagship store in NYC except for a sliver of land that holds Macy's giant billboard. Macy's has lost the lease on that land. Amazon wants to advertise there now.
  - Often bills in Congress will have deadlines by which they must be voted. But the House can circumvene this quirk by never adjourning the session. In other words, this past Friday was still actually Thursday in legislature time.
  - The Monday Night Football game was delayed because of lightening. The game was in a domed stadium albeit with open sides.
  - The US buys cotton products from China which gets much of its raw cotton from the US (the US has banned imports of cotton products that are made with slave labor in Xinjiang).
  - The last time oil prices were this high (2014), there were about 1100 active drilling rigs in the US. Today, there are 428 rigs at work. Oil (crude and petroleum products) Inventories are about 20% higher than in 2014.
  - A Dungeons & Dragons "streamer" has made $9.6mm in the last two years.

- Descendants of a black (Black) family whose land in southern California was taken under imminent domain are getting a parcel of beach front property worth $75mm.
- The arcade boxer in *Mike Tyson's Punch Out,* Soda Popinski, was originally named Vodka Drunkenski.

*There is an interesting working paper from the Fed right now. It contends that inflation expectations do not, indeed, factor into actual inflation numbers. We find the paper confusing and without much merit. But we will certainly defer to the peer review.

Trading: We used the market dips to nibble on some of the Reopening themes we like. Our Gross Exposure is still near the lowered end after we deleveraged a bit in the 3Q. We will continue to buy any random dips. We trimmed a touch of our oil exposure. We will trim more of this if the rally continues, but we want to remain long. We are also adding to our Put protection on the junkier High Growth names. We think the days of the speculative fever might be behind us.

TSLAQ: Tesla lost a racial harassment lawsuit. The jury awarded the black man $130mm. For some reason the Wall Street Journal capitalizes the word "Black." We do lots of nonstandard capitalizing, but that is to emphasize specific Wall Street terms which can be confusing. We do not think the WSJ capitalizes "white" people. Nonetheless, the stock rallied on the news. In other weird Elon news, apparently there is another fake cryptocurrency. The SHIB token was made up following tweets from Elon about his Shiba Inu dog. Elon has pumped this token up to $13b worth. God help us all.

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