

For the Record

For the Record

Since it is the start of the year, it seems like as good of a time as any to put a few things on record before diving into the meat of this T-Report. There are things that I want to refer back to over the course of the year because they relate to the business of strategy.

For the Record #1

Everyone hates strategists who claim to have called every move correctly. I can guarantee you that if someone called every move right in the markets, they wouldn't be sitting in front of a computer typing missives because they'd be bazillionaires!

A close second for the most annoying behavior by strategists is touting their good calls and completely ignoring their bad calls (Bitcoin is back to \$21,000 this weekend).

Some of this is human nature. We all "want" to be right and all tend to emphasize the "good" rather than the "bad".

For the Record #2

Many of our readers have P&Ls. That is a discipline like no other and while I try to think of our strategies in terms of P&L generation, risk management, etc., it isn't the same as having an actual P&L.

Having said that, we have people who live and die by daily/weekly/monthly P&Ls (which is ideal for Bloomberg IB as a form of communication). We also have people with weekly/monthly/quarterly timeframes (the T-Report is geared for these people). Finally, we have some who even think in years (which seems important for corporate strategy, but it is difficult to manage a portfolio around).

For the Record #3

One thing that strategists dislike is when people discuss their "idea" with them but don't realize that it was the strategist's "idea"! That is largely a failing on the strategist's part. Either the work isn't getting distributed well enough (a good time to check mailing lists, ensure things aren't going to junk, etc.), the work/titles are too confusing (though I'm not sure I could live without writing [I Like Big Banks and I Can Not Lie](#)), or I just need to write more clearly.

Last weekend's [A Simple View](#) is part of the process of addressing this issue going forward. [8 Seconds](#) served the function of letting people know that our positioning had changed, but maybe the title was confusing (though the image of trying to ride a wild bull felt "informative" to me).

Finally, while the Fed is apolitical, I couldn't help but send out the [Shifting Politics](#) of Inflation on Friday, because that has the potential to shift the national narrative and could either influence the Fed or (at least in the case of the WSJ) might be the conduit the Fed is using to signal a change.

On the Record

We will "subtly" shift from "for the record" to "on the record".

Rachel Washburn hosted a fun and interesting webinar on Friday that started with World War III possibilities but ended in a better place. Generals (ret.) Walsh and Marks were spot on, and I was able to add a few points on how their geopolitical input is impacting our macro market and economic outlooks (replay will be available shortly).

Academy was one of three firms that participated in Friday's half-hour [Real Yield](#) show on Bloomberg

For the Record

TV. You know a show covers a lot of fixed income ground when CLO ETFs get mentioned and it seemed to be a fluid part of the conversation (rather than forced). Some really interesting views and ideas from the other guests made this a great show to watch if you have about 20 minutes or so this long weekend.

On the Road

My favorite part of my job has kicked off in earnest! From D.C. and Princeton last week, to San Francisco, Palo Alto, Newport Beach, and San Diego this week, seeing clients is back in vogue. There is nothing more fun than sitting with people in a variety of jobs/industries and sharing ideas. I’m even excited for Minneapolis in early Feb (it will be cold, but should be fun) and look forward to another opportunity to speak to a group of municipal issuers in Alabama!

Travel and seeing such a diverse group of people allows me to learn about so many aspects of the economy and it makes my job so much easier!

Consensus is Neutral

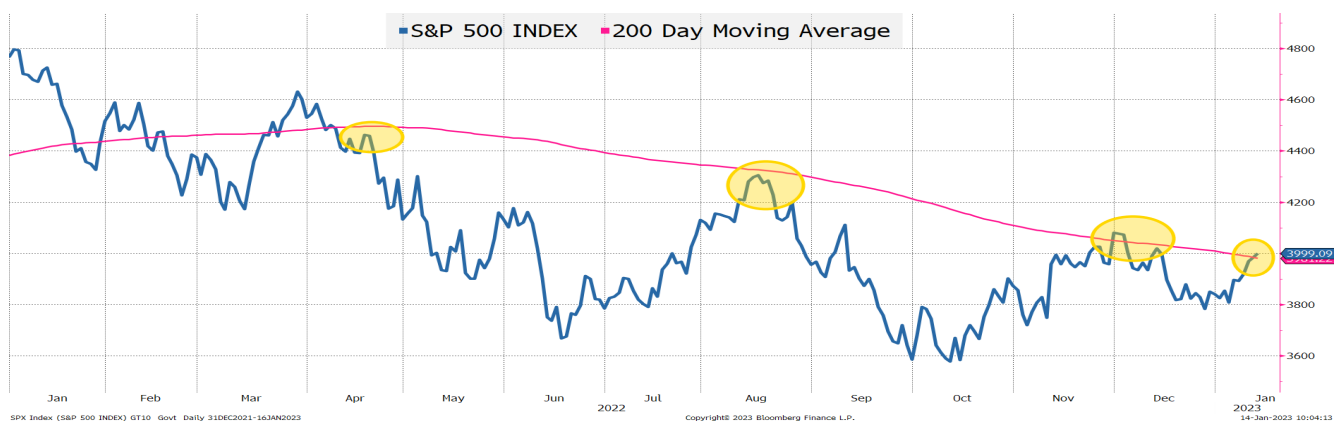
Back to the meat of the report.

If I’ve done a good job explaining myself this year, you should know that I’m basically neutral on stocks, bonds, and credit here. That view seems to be rather consensus.

The [CNN Fear & Greed Index](#) has bumped up to 63 (which is technically in greed territory, but just above neutral).

The [AAI Sentiment Survey](#) is in neutral territory (though very close to being too pessimistic). What was most interesting is that the number of bears has dropped from 52.3% to 39.9% since December 21st, but almost all of those people piled into the “neutral” camp as the number of bulls remained quite low.

I’m not big on technical charts, but this chart sticks out so much that I couldn’t help but use it to illustrate my “neutral” point (I’m not opposed to charts, but they just aren’t my first choice of things to highlight).



The S&P has snuggled right up against the 200 day moving average. From my limited understanding of charts, this is a crucial level. The S&P has failed to breach the 200 DMA since the sell-off took hold in late March. It could easily be rejected again. On the other hand, if it breaks through, we could see buyers emerge. Not only from all of those positioned as “neutral”, but from bears and particularly CTAs which have a reputation for being formulaic/algorithmic and tied to big levels (like the 200 DMA).

So maybe I should refine my view from simply “neutral” to “neutral, waiting to pounce on the next move – if only I knew what that next move would be”.

For the Record

Even though at the start of today's report we wrote about providing more "clarity" on views, I'd lean towards owning some tail risk in either direction! If we fail around here, many could press shorts and get out of recently acquired risk. If we break above, the opposite happens.

Yes, at some level this happens all the time, but the "neutral" positioning coupled with a major, very visible level (which happens to coincide with the big round number of 4,000) makes the next few days particularly interesting for me!

What's Next for Inflation?

I think that inflation will continue to fall and we will see more monthly CPI prints that are negative and even Core CPI will have a negative print this quarter.

Many disagree, but I think that with Q4 coming in at 0.8% (3.2% simply annualized) we've "beaten" inflation.

What Will the Fed Do?

I'd be shocked if they did more than 25 bps at their next meeting.

Yes, they will talk about "financial conditions" (aka the S&P 500), but they are starting to get the political and media aircover to back down from 50 bps and some of their higher terminal rate calls.

There are still over 2 weeks until their meeting and we will get more data. I'm betting that if anything, that data steers them to "25 bps and done" messaging (probably too late for them to do zero, which is what I think that they should do).

The Fed will NOT be quick to cut. They should stop hiking, but even I'm not advocating for cuts (it would have been easier if they started on the glide path to stopping rate hikes a few meetings ago).

They will continue to do QT. This, to me, acts as an anchor on markets as every month we need to absorb more bonds from the system than if QE had not started in the first place. Why QT gets so little attention still baffles me.

The Bank of Japan is expected to let the 10-year yield rise to as much as 1%. I view this as "on par" with QT. It is another drag on asset prices in the U.S. as Japanese investors can allow some of their FX hedged/dollar denominated bonds to roll-off when the hedges come due and just buy domestic bonds. It isn't alarming and won't be all at once, but it adds to the pressures of finding dollar denominated asset buyers. With the 10-year bund at 2.16% this is already happening in Europe, but it also tells me that **1% is probably getting to the low end of the range that the JGB 10-year would naturally trade at** given their domestic savings rate and still low levels of inflation.

What Will the Economy Do?

Yes, jobs still seem good, but that isn't as important as it should be.

What I'm seeing is a couple industries acting as the epicenter of the problems for the economy!

Big tech, fueled by everyone (from private equity, to vehicle manufacturers) took 5 steps forward in the past few years! Will we see one or two steps back as companies become more cost conscious and not every tech investment will be cheered by equity holders. Have manufacturers changed what chips they rely on as they've battled supply chains? **Without a doubt, in 5 years technology will play an even bigger role in society and the economy**, but it doesn't mean that we haven't already priced too much in.

For the Record

I see a potential problem in this market that it is radiating out. The local economies are incredibly interconnected.

The **homebuilder** ETF (XHB) is up almost 20% in the past 3 months! This is a contrarian play that I probably should have gotten on board with, but this is an industry still in the early stages of digesting the spike in mortgage rates and overall loss of wealth in this country. I'm keeping an eye on this.

We will get some clarity and resolution on the inventory side of the equation in the coming weeks as we get the regular data and we also have companies discussing it in detail. I'm not optimistic, but maybe this will be a pleasant surprise.

Services could be the key. Was the print that we highlighted last weekend an anomaly or a harbinger of more bad news? Even as a bear on the economy, that data seemed surprisingly weak, so I expect something not quite so bad, but "less good" than most bulls are building into their forecast.

What About Earnings?

I will start by quoting my friend Peter Boockvar. He "guarantees" every quarter that about 70-75% of companies will beat earnings. His point, as I take it, is that expectations get pushed down to the point that most companies beat them, so there is little to be gleaned from the parade of "beats" that we will get.

We will all be listening to how CEOs portray their vision for the rest of the year. Their views will mean a lot, but they usually do.

My gut is that they will be more cautious than expectations, in part because some of the "wobble" room that they had late last year has already been used. Also, they are in jobs where they want to outperform expectations, and even if your company is doing well, you might be cautious because you see companies around you going through tougher times.

The one thing I "know" for certain is that we will get a lot of chatter about stock repurchases post earnings announcements and unless something changes, that will help support equities.

It's a Moving Picture, not a Snapshot

The biggest mistake people may be making is looking at the data as though it is static.

If we take a **snapshot of recent data**, it is easy to craft a "**soft**" landing narrative.

But we don't live in a static world. Decisions made months ago (on the policy side, on the household side, on the corporate side, etc.) take time to play out. It would be fun if economists could drive the economy like a jet ski, but it is a huge tanker, and once underway it is difficult to turn or even change speed.

So, I 100% agree that the current data has a "soft" landing feel, but I don't believe there is a chance that the weakening of economic data (alongside lower inflation) will stop here!

We had to be setting up to "catch" the fall here, and if anything, we are still pushing on this well past the point we should be.

Maybe I'm wrong here, but simple Newtonian physics tells us that an object, once set in motion, will stay in motion and that is what the Fed has done and we are going to blow right through the "soft" landing station and enter into some unsafe territory.

For the Record

Bottom Line

Stocks

- **Neutral.**
- Own options that cost very little, but generate profits if the S&P 500 breaks 4,100 or 3,900 by the end of next week (yes, resolution will be rapid and I hope that I don't miss it between now and when futures open, let alone in the actual market).
- **"Gun to head"** I'd bet that the rally continues and we test 4,200 on the S&P 500 which means I've got to get back on that bucking bronco (or I got off too early).
- **We will break 2022's lows**, but that isn't my gut for the next move.

Rates

- **The 10-year at 3.5% isn't particularly appealing.** We should see corporate issuance spike after earnings announcements. 3.5% is quite inverted versus the front end with a Fed that will hike at least 25 bps more. The BOJ won't help things. Positioning has become a bit bullish on bonds (at least from the chatter I hear). So, even in my deflationary view, I would not be long 10s here.
- **I like 5-years better than other points.** It is "only" 3.6%, so not much of a pick-up, but I like the risk/reward better in 5s. Maybe, the 2-year is more obvious, but it has so little duration and if I'm right and the Fed won't hike (but also won't cut), then there isn't a lot of room.
- **For now, I'd be short Treasuries/sovereign debt.** Yes, I think that deflation will be the discussion point of this quarter, but for now, I just don't see much value in sovereign debt.

Credit

- **A "weird" barbell.** I'm most concerned about **leveraged loans** (more so than high yield, because of the type of issuer that tapped that market, versus the bond market), but I like "senior" tranches of **CLOs** (anything IG rated and even BB). It is difficult to go lower in the cap structure of CLOs given the fact that the building blocks are my least favorite part of the credit market. Prices of various CLO tranches have bounced nicely in the past couple of months and new deals could accumulate some good collateral at really interesting levels.
- I'm "meh" on high yield and even investment grade.
 - High yield is so hated but while it is interesting, the combination of rate risk and credit risk isn't a screaming buy to me (though certainly more of a buy than leveraged loans).
 - Investment grade is ok, but I think if Treasury yields rise, spreads will contract by 25% or so of the move in Treasuries, so I expect higher overall yields and lower dollar prices. If sovereign yields drop, spreads will widen on at least a 50% basis (if not closer to 100%). So, in a falling yield environment, IG yields won't change much and dollar prices won't do a lot (kind of a difficult risk/reward to pitch).
- **So, I am equal weight IG and underweight sovereign debt. I am underweight leveraged loans and would use those funds to buy CLO tranches or some high yield bonds instead.**

That's what I've got for now! Will be an interesting week or two and it is difficult being so bearish on the economy, but neutral (and maybe "gun to the head" bullish) on risk in the very short-term.

Have a great long weekend and hopefully we can connect during my travels this year!

For the Record

Disclaimer

This document and its contents are confidential to the person(s) to whom it is delivered and should not be copied or distributed, in whole or in part, or its contents disclosed by such person(s) to any other person. Any party receiving and/or reviewing this material, in consideration therefore, agrees not to circumvent the business proposals explicitly or implicitly contained herein in any manner, directly or indirectly. Further, any recipient hereof agrees to maintain all information received in the strictest confidence and shall not disclose to any third parties any information material to the opportunity contained herein and, upon review hereof, agrees that any unauthorized disclosure by any party will result in irreparable damage for which monetary damages would be difficult or impossible to accurately determine. Recipients recognize, and hereby agree, that the proprietary information disclosed herein represents confidential and valuable proprietary information and, therefore, will not, without express prior written consent, disclose such information to any person, company, entity or other third party, unless so doing would contravene governing law or regulations.

This document is an outline of matters for discussion only. This document does not constitute and should not be interpreted as advice, including legal, tax or accounting advice. This presentation includes statements that represent opinions, estimates and forecasts, which may not be realized. We believe the information provided herein is reliable, as of the date hereof, but do not warrant accuracy or completeness. In preparing these materials, we have relied upon and assumed, without independent verification, the accuracy and completeness of all information available from public sources.

Nothing in this document contains a commitment from Academy to underwrite, subscribe or agent any securities or transaction; to invest in any way in any transaction or to advise related thereto or as described herein. Nothing herein imposes any obligation on Academy.

Academy is a member of FINRA, SIPC and MSRB. Academy is a Certified Disabled Veteran Business Enterprise and Minority Business Enterprise and is a Service Disabled Veteran Owned Small Business as per the US SBA. Investment Banking transactions may be executed through affiliates or other broker dealers, either under industry standard agreements or by the registration of certain principals.