This Week in the Markets

Stillwater's *"This Week in the Markets"* returns, just in time for what should prove to be a defining year for the economy and the longest bull run in its history, that is up until October 3rd of last year. While you needed to squint before to see signs of top down trouble in the U.S., in emerging markets, China, and developed Europe, at present the waves are not just on the horizon, but right square in front of us all now.

'The Great Wave'

Source: Tech Crunch

With the exception of a great interview David Rubenstein conducted with Fed chair Jay Powell at the Economic Club of D.C., it was a week light on market moving economic news. With this as our backdrop, we are going to kick off with a look back at what went right and what went wrong for us in 2018.

For a whole bunch of good reasons, including regulatory requirements the SEC lays down, Stillwater does not make individual ‘buy’ or ‘sell’ recommendation. Instead we provide a transparent look into what we’ve seen and done in the portfolios we manage on a weekly basis. If you like what we are writing, and the ideas we are putting to work, consider becoming a client.

What Went Right

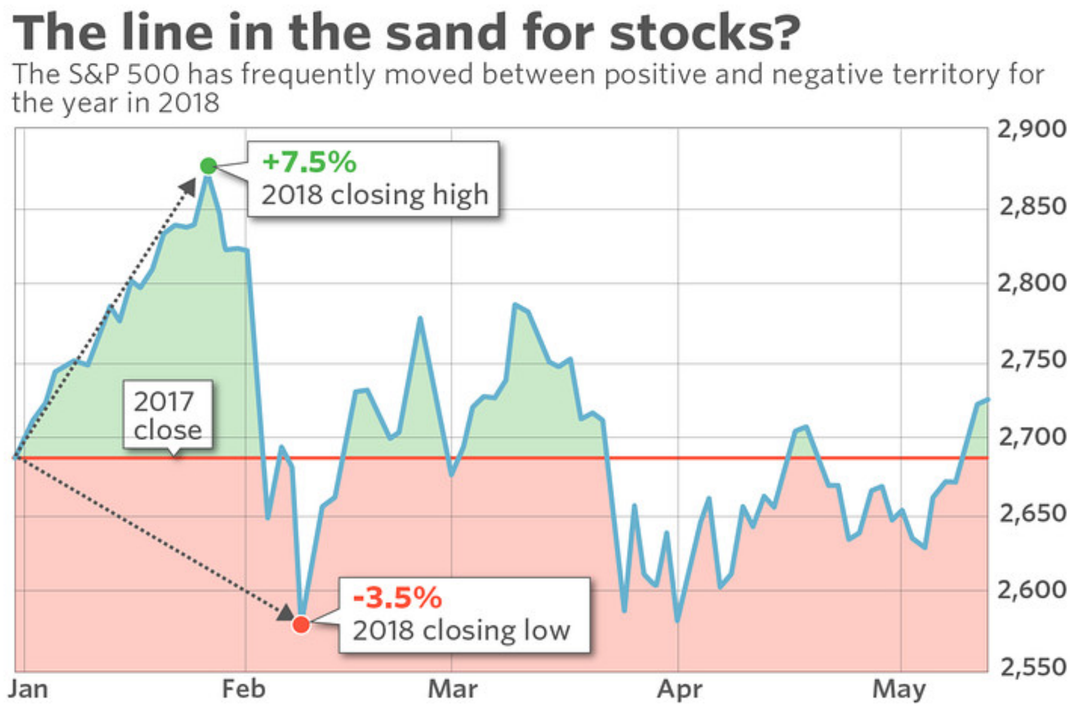
Our single best idea of the year was to short Facebook after the Cambridge Analytica trouble broke. To be clear, there was no real edge to this call except for the fact that we didn't think Wall Street really knew what they had bought into, and of all the FAANGs, this company was the one least needed by its users. Therefore it doesn't surprise us at all that Facebook is being compared to a cult inside the walls.

"Somebodies watching me…"

Source: Security Affairs

In terms of overall market moves, February was a month that shined. While our core strategies missed some of January's parabolic move higher, we were well positioned for any downside. This paid off with a smooth ride, and an up month, while the markets were down 5% to 10%, depending on which one you were looking to compare us to.

An 11% Tip-to-Tail Selloff



Source: Market Watch

There was a bull market in herbs and spices this year, as industry leader McCormick outperformed almost everything else in the market. In 2018, the company saw a 50% rise in share price, part of this was due to the stable nature of the business and consistent dividend growth. More importantly, the company completed the successful acquisition of Frank's & French. For those not in the know, French is the mustard maker, and Frank's makes hot sauce that goes really well on wings.

What? No Cumin?

Source: McCormick

Right then Wrong….or Wrong then Right

Oil & gas was particularly challenging last year. Commodities have a long tradition of being the place you want to be late in the cycle, and crude is most certainly the biggest global commodity of them all.

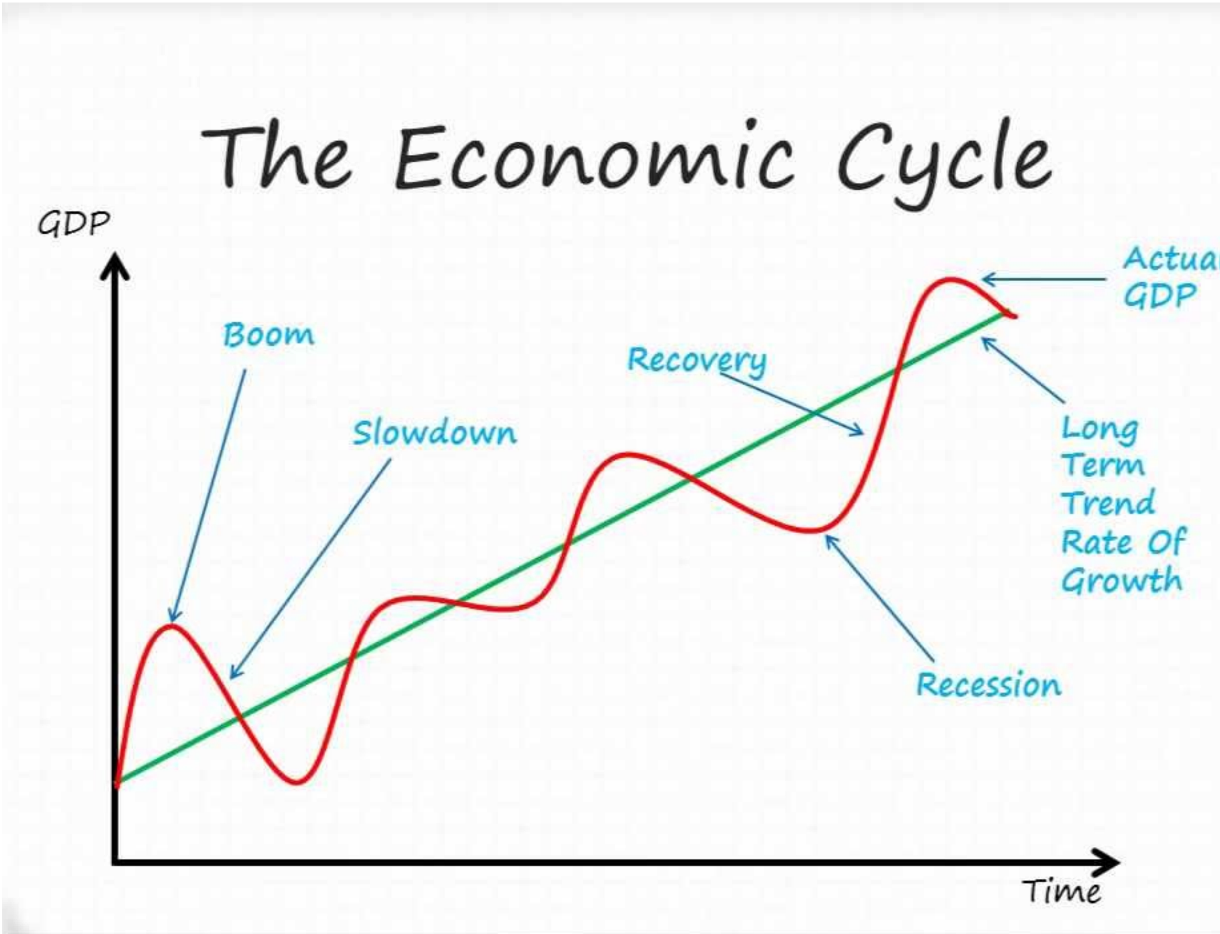
Coming into 2018, the year exploration, production, and oil service were unloved and vastly under-owned. In our all-weather portfolio, we leaned long the group, and it paid off through the first ten months of the year. And it continued to work until president Trump decided to pull the rug out from under Saudi Arabia by extending a production lifeline to Iran, claiming victory for the U.S. consumer as crude prices suffered their worst selloff in more than a decade.

WTI Crude

Source: Macrotrends

For much of the last two years, we have been trying to figure out the "where are we" puzzle in terms of the economy. For much of that time we leaned towards it being late cycle. And it wasn't until April and May we scaled that back and began to believe that we weren't as late as we thought, tilting the all-weather portfolio more towards growth. This worked remarkably well for five months, and our returns reflected it.

Economics 101



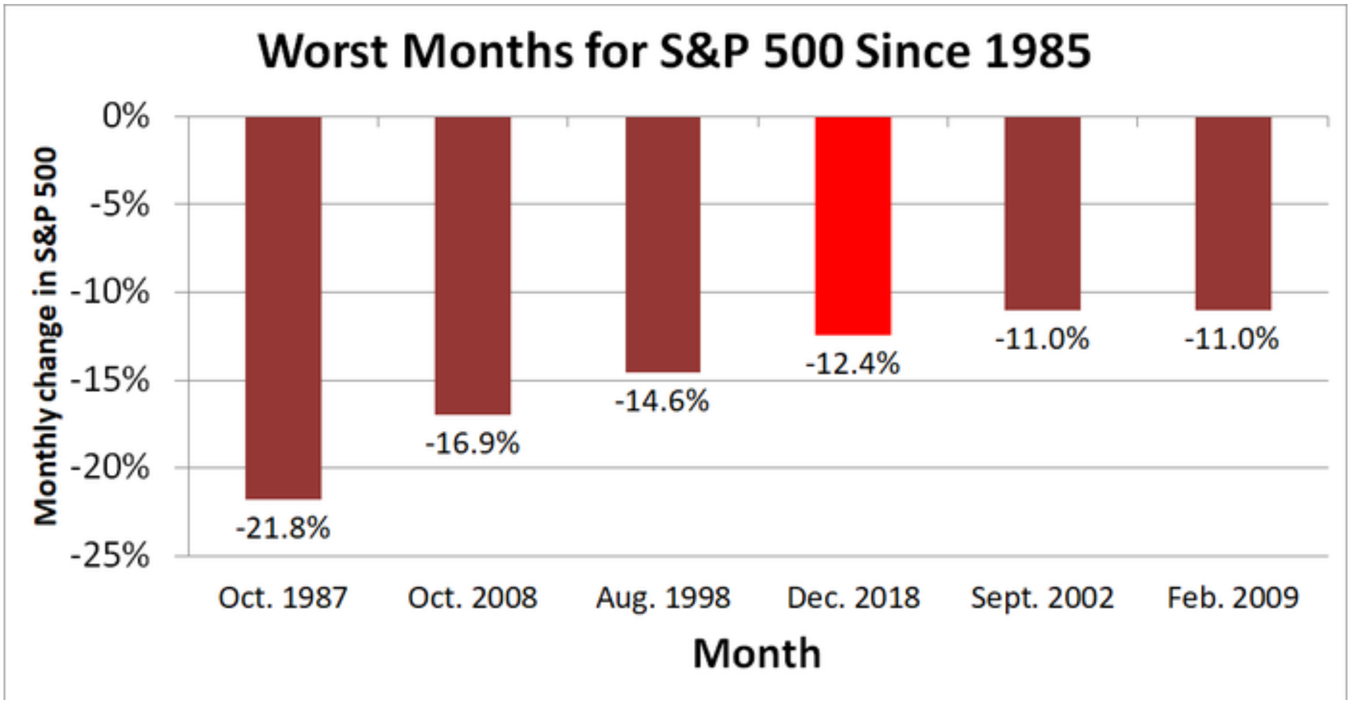
Source: YouTube

On October 3rd, the markets began to discount a different scenario, and one that had us end of cycle. We understood the premise, but held to our belief that our economy continued to look like it was on solid footing. Up until this point, we were flat on the year in our hedged growth strategy and up well ahead of our benchmark, and our competition, in our conservative hedged equity income product. And then December hit.

What Went Wrong

We, like a lot of others on Wall Street, didn't properly discount that the worst December since the Great Depression was headed our way. For all intents and purposes, it felt as though much of the selloff in October and November re-set valuations, and more importantly expectations for what was baked into the market. The market isn't always right, but the market is the market, proving this once again in December 2018 by ranking itself amongst the worst in history.

Bad Omen



Source: The Motel Fool

Though it's not at all professionally enjoyable to miss a month like December, it is not our biggest regret of 2018. That honor is reserved for the many fat pitches the market gave us on the short side that we were only able to manage a single or double out of the opportunity. From housing, to autos, and some select retailers, we had a lot of great ideas. That being said, this was a year when action coming from the short side of the mound looked like gopher balls getting served up during batting practice.

Fat Pitches

Source: The Star Tribune

The Bottom-Up

The last quarter, specifically December, proved to be a pivotal moment for how the markets, and how they would react to what we thought was a pretty well advertised earnings recession coming in 2019. Turns out we were wrong, and that cost us in our equity strategies.

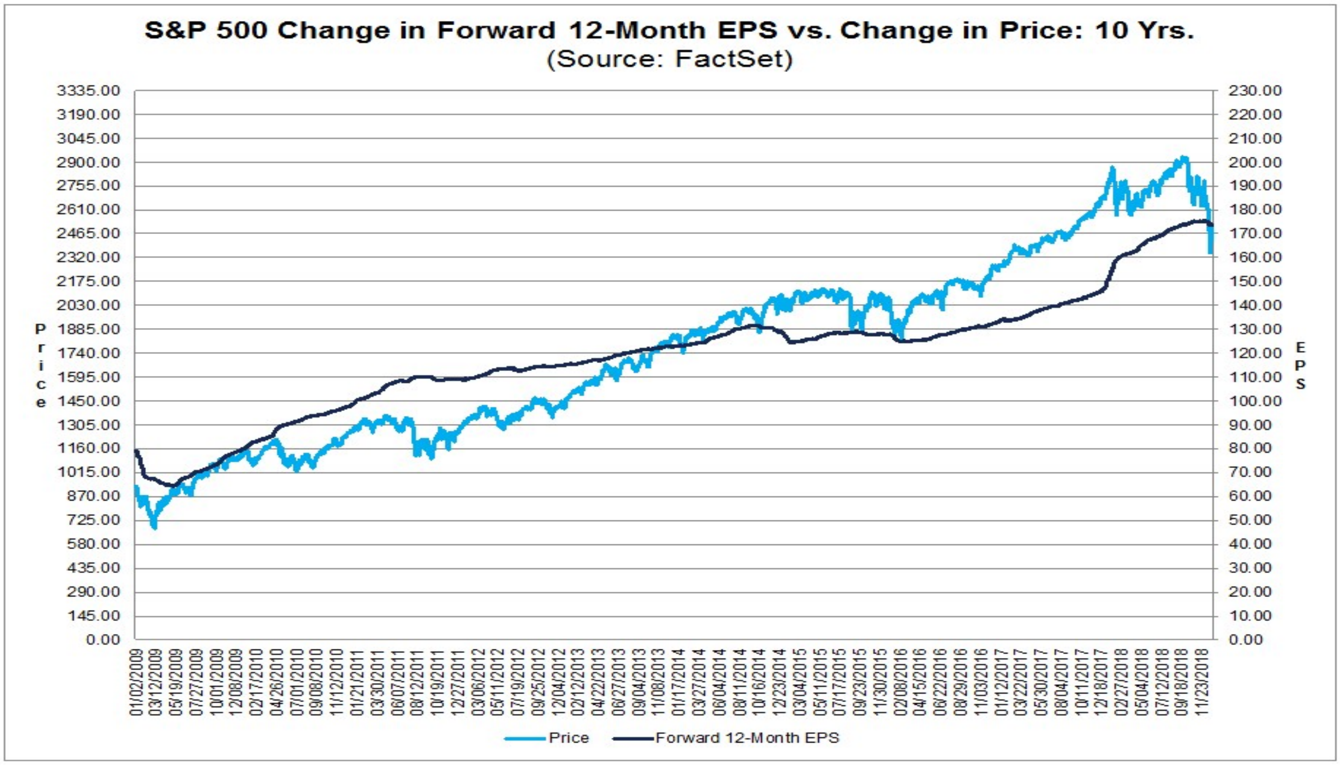
The challenge has been knowing when you are. This year, conditions turned on a dime at the start of the fourth quarter, with a crescendo in December. And while we live by the mantra that there are "no crybabies in the casino", the deck the market was dealing from went from face cards all around, to splitting twos. And nobody wants to be at the table with those cards.

A Full Deck

Source: Thought Co.

The *Wall Street Journal* ran a great article on the difference between an earnings recessions, and a real one, the punchline being sometimes they line up, and sometimes they don't. Which of course isn't very helpful news for those of us trying to make money late in the cycle.

FactSet provides a great resource for those who want to follow the data more closely. Each week they produce a report entitled *"Earnings Insight"* which takes a deep dive on profits that have been reported, and those that are expected to be released. You need to go back three years to 2016, to see the impact of an earnings recession, and in the fall of that year, Donald Trump would be elected president, and it was off to the races for stocks and earnings that were juiced by big tax cuts.



Source: FactSet

Private Companies

WeWork isn't working anymore, at least if you use Softbank's pocket book as the barometer. This week it was announced the office sharing startup would only be seeing a $2 billion investment from the fund, not the $16 billion Masayoshi-Son wanted to send its way. That dropped the valuation from $45 billion to $36 billion. A billion here, a billion there, pretty soon you are talking real money.

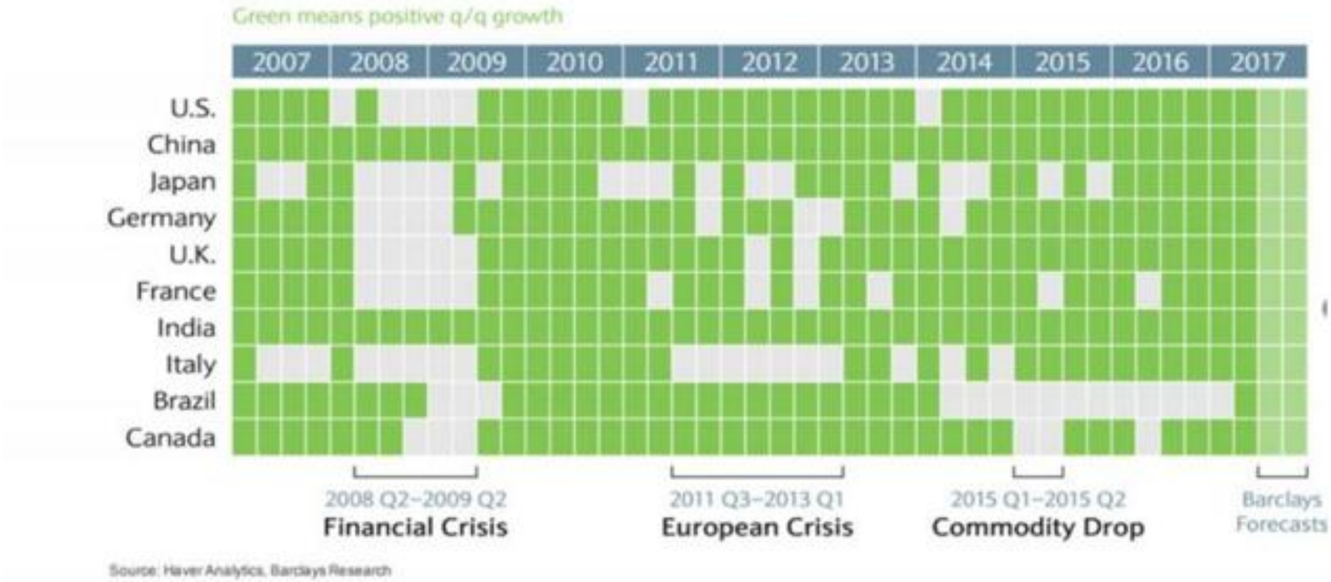
WeWork Manhattan

Source: The Wall Street Journal

Gundlach's "Just Markets"

Our favorite prognosticator on the economy and markets, Jeff Gundlach, hosted his annual *"Just Markets"* presentation on Tuesday. During the call, Gundlach acknowledged that the predications he made last year were pretty good. The fine people at *Bloomberg* scored it with an 80% success rate. Seeking Alpha also gave their own rundown of this year's perspectives. To show that it's a changed world, this time last year it was a full on green light for global growth.

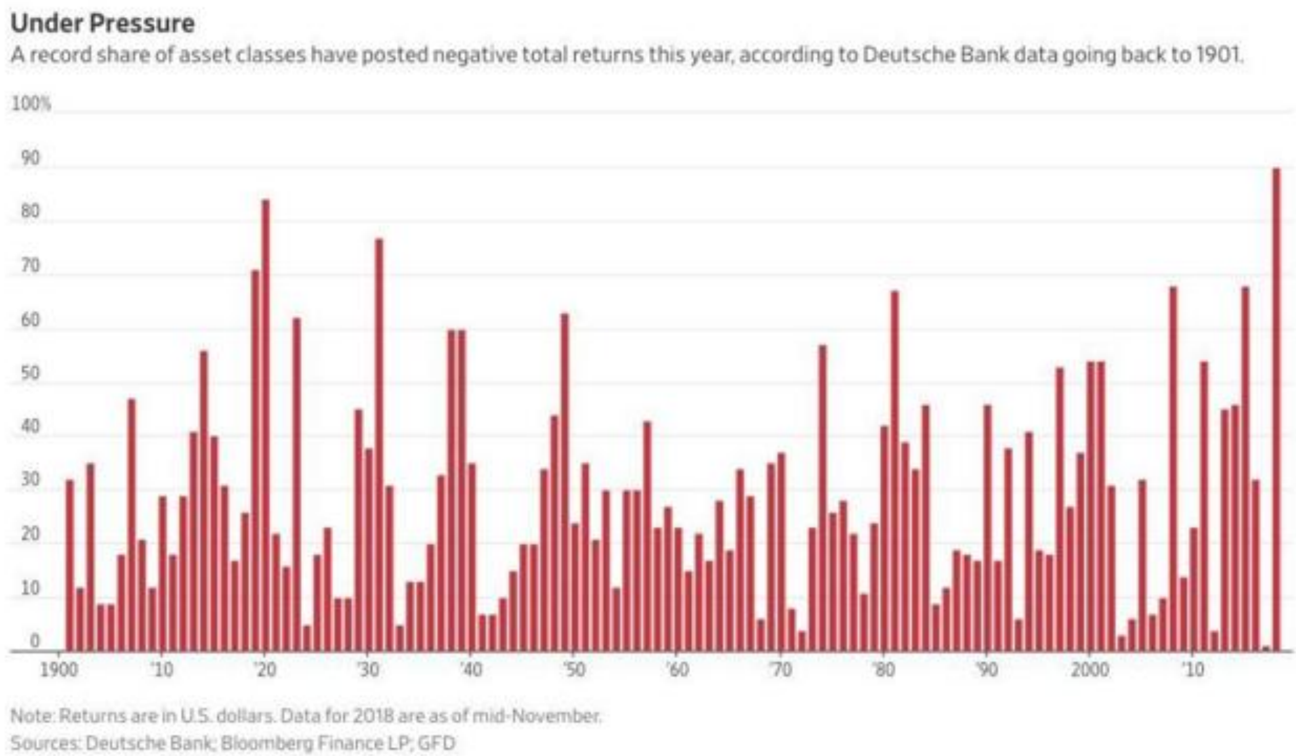
"We are go to throttle up."



Source: DoubleLine

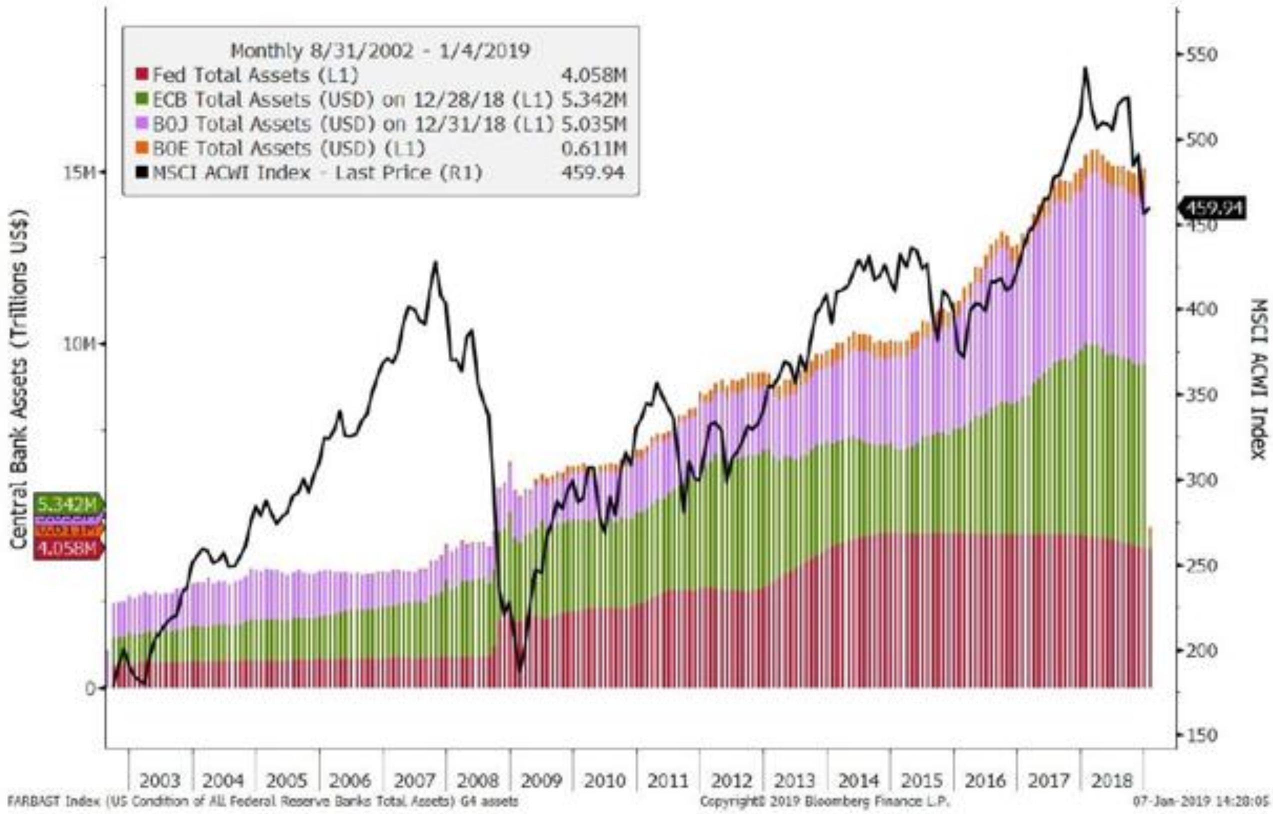
To show you how quickly markets can show their fickle side, 2018 wound up being a year when nobody made money, at least no asset class did. Keep in mind, this data series below goes back 110 years.

It Was a Good Run



Source: DoubleLine & Bloomberg

While this year's observations were a little more pedestrian than lasts, once Gundlach got to the subject of exploding government debt, he was downright breathless. Bottom line, he sees a huge problem that is not priced in and he thinks the Fed is on a 'suicide mission'. Jay Powell thinks government debt is a huge problem too, but we are pretty sure he doesn't go to the same extent and think the latter.



Source: Bloomberg & DoubleLine

Diversions – January Real Estate

While new home sales may be plunging, listings for old homes seem to be picking up. Stillwater gives you a special look into some of the more noteworthy and gentrified properties on the market.

The 222 year old John Abbot House in Andover, Maryland can be had for $1.75 million. The home sits on 2.5 acres, is 5,000 square feet inside, and contains 8 fireplaces. It is walking distance to Andover Academy. If you and the seller square on a deal, you will be the fourth owner in the homes history.

Not Bad…For Its 222 Year Age

Source: Christies Real Estate

A sprawling mid-century modern home, the Frank Sinatra once called home, has hit the market for a cool $12.5 million. Overlooking the sprawling Chatsworth Nature Preserve, the home has 8 bedrooms and 8 baths inside it’s 8,000 square feet of space. Marilyn Monroe called the guesthouse at Byrdview home.

Mid-Century Masterpiece

Source: Architectural Digest

Manhattan’s famed Chrysler Building is on the block as the Abu Dhabi investment authority looks to recoup the almost $1 billion it paid at the top of the market in 2008. Built between 1928 and 1930, the title of Worlds Tallest Building would only last one year as the Empire State building would overtake it in 1931. The Gargoyles come with the purchase price.

Shiny Objects

Source: The New York Times

While the property closed four months ago for $28 million, the story of the famed 'Canary Cottage' on the Monterey peninsula are worth a mention. The property sits due west of the Lodge at Pebble Beach, and has been home to some savory stories of gambling and bootlegging back in the day. When it was still on the market, you could rent the house for an undisclosed sum, which CBS did almost every year when they broadcast the Pebble Beach Crosby Clambake.

The Canary Cottage

Source: Estately

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