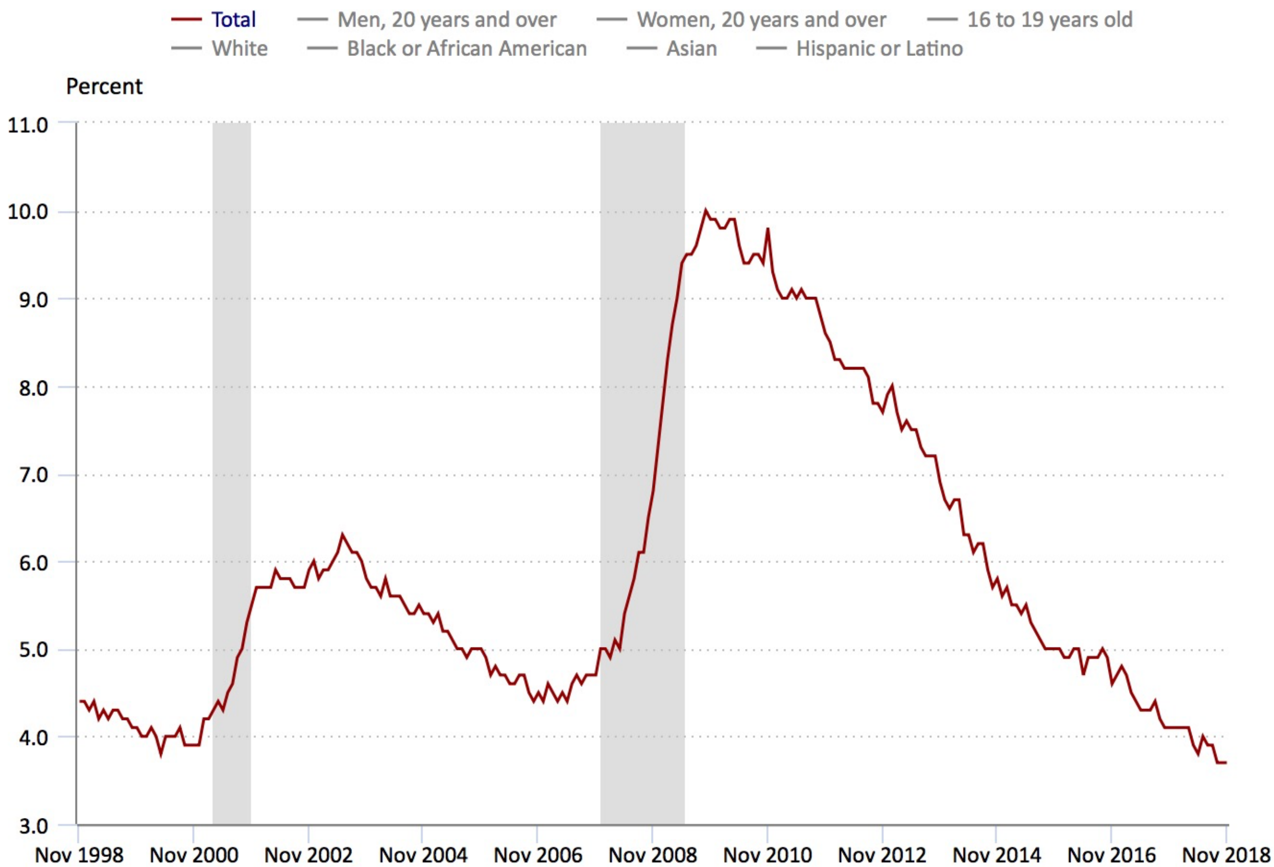
This Week in the Markets

The Economic Top- Down

The November employment report came in on the cool side, with the addition of 155,000 new workers. The market was expecting something closer to 200,000, and October was revised downward. The culprit being the increasing uncertainty surrounding global trade, that said, the case for Powell to stand down on hiking rates just got better.

Civilian Unemployment



Source: The BLS

Markets went from flying higher on Monday, to falling through the floor on Tuesday and Thursday. The reason ostensibly being the reality that our shoot from the hip Commander in Chief took it further out on the left tail, and is now simply making it up as he goes. The catalyst? A tweet from Trump that a deal with China had been made, when indeed none existed.

Understand, we're not looking to take this conversation in a partisan direction. We, along with everyone else who are trying to figure out the markets and protect client capital, are simply frustrated that big moves are being driven by news that seems to fall from the ether. More importantly, we want to see this economy keep growing for as long as it can. It takes a smooth hand on the throttle to do so at this point in the cycle.

Xi and Trump at the G-20

Source: South China Morning Post

The situation with China worsened when it was revealed that the CFO of Huawei (waah-way) was arrested in Canada on charges she had violated U.S. sanctions against Iran. The Chinese government called the arrest “despicable hooliganism”. This is no small matter as the company is one of China’s most important, *CNBC* takes you inside.

Huawei in Shenzhen, China

Source: CNBC

Some observers would call Trump's announcement that a "BIG" agreement had been made contradictory and confusing, while others called it a flat out "mistake". Either way, trying to manage an up 3% day, followed by two down 3% days, is no way to make a living.

If *CNBC's* John Harwood is correct, portfolio managers won't be the only ones finding it hard to make a living, as it's looking increasingly likely that president Trump could possibly be the second president after Jimmy Carter to seek re-election during a recession.

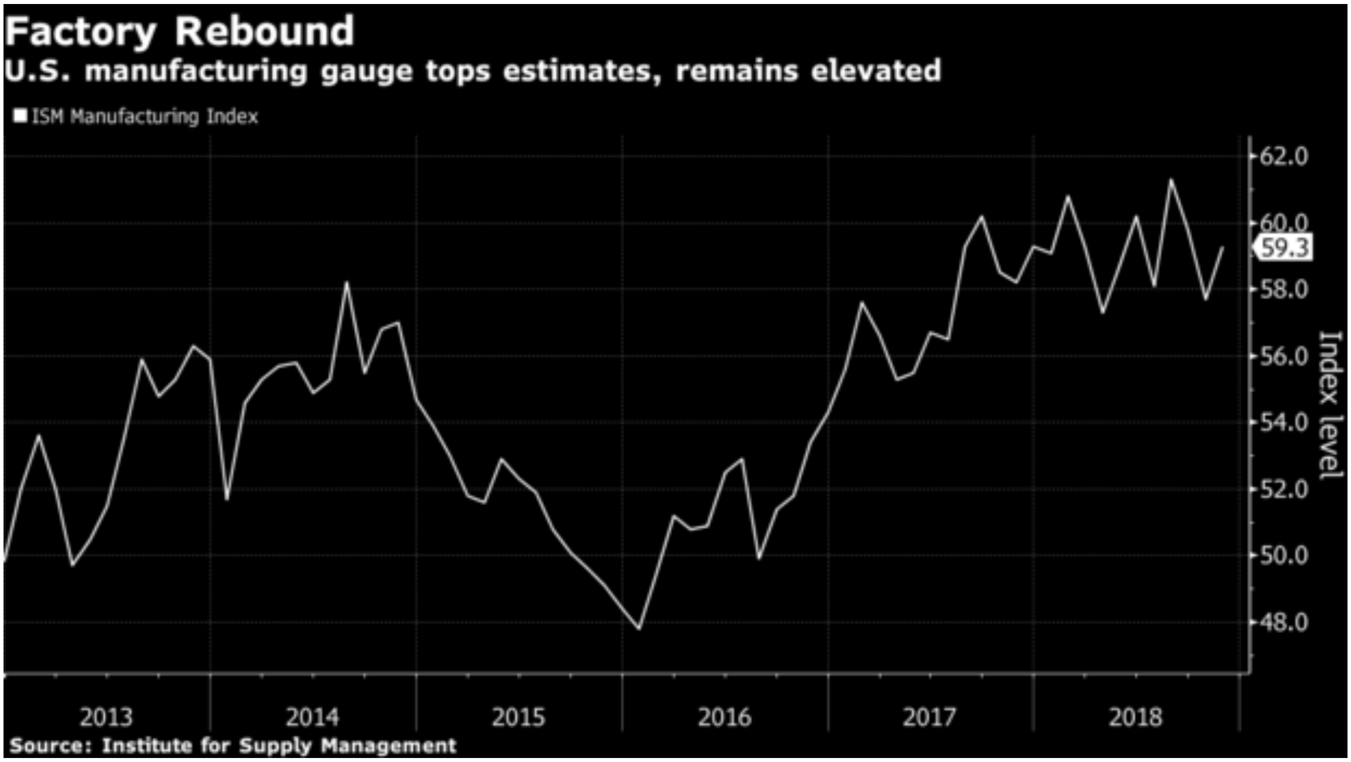
The upside is that we got a new nickname for the president. For those left of center, or just wanting some comic relief from the situation, look no further than the *Late Show's* Steven Colbert to rail on our new "Tariff Man".

"Tariff Man"

Source: Market Watch

Let's venture outside of the rhetorical world and into the real one, the industrial economy appears to be holding up. We were reminded of that this week when the Institute of Supply Management reading of the sector's strength printed at 59.3, anything above 50 is meant to show economic expansion.

ISM Still Holding Strong



Source: Bloomberg

In news that is telling to how challenging this year this has been, the number one asset class so far is, wait for it, cash! Goldman Sachs thinks this trend continues into 2019, and investors should expect ‘low returns’ across the board.

It’s All About the Benjamins

Source: Forbes

The yield curve, or at least part of it, finally inverted. Causing every market analyst and their brother, mother, sister, and daughter to opine on what it means and when we can expect the next recession to hit. A man whose opinion should be taken seriously, DoubleLine's Jeff Gundlach, says this is a signal 'that the economy is about to weaken'.

Inversions Happen

Source: Bloomberg

There are clearly outside forces at play with this market, as the time from inversion to market tops can be anywhere from 12 to 24 months. In fact the last time this happened in 2006, the market produced a 15.61% return. The following year, the return was more muted at an increase of 5.48%. Both of these years were bit players in the grand global financial crisis production, as the S&P 500 would go down by 36.55% in 2008.

Harrowing Days for Wall Street

THE WALL STREET JOURNAL.

DOW JONES — A NEWS CORPORATION COMPANY

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Last week: DJIA 11421.99 ▲201.03 1.8% NASDAQ 2261.27 ▲0.2% NIKKEI 12214.76 unch. DJ STOXX 50 2858.68 ▲3.8% 10-YR TREASURY ▼20/32, yield 3.730% OIL $101.18 ▼$5.05 EURO $1.4217 YEN 107.87

Crisis on Wall Street as Lehman Totters, Merrill Seeks Buyer, AIG Hunts for Cash

U.S. Opts to Avoid Lehman Rescue, Stirring a Momentous Weekend for American Finance; Traders Brace for a Chaotic Monday

BY CARRICK MOLLENKAMP, SUSANNE CRAIG AND SERENA NG

The American financial system was shaken to its core on Sunday. Lehman Brothers Holdings Inc. faced the prospect of liquidation and Merrill Lynch & Co. was close to a deal to sell itself to Bank of America Corp.

The U.S. government, which night, Bank of America was close to striking a deal to buy Merrill Lynch for about $44 billion, or $29 a share. Lehman was working on a possible bankruptcy filing.

As worries spread across Wall Street that Lehman wouldn't survive, brokerage firms, hedge funds and other traders moved to disentangle themselves from trades with Leh- turned to Merrill Lynch, which boasts the largest force of retail brokers, and to American International Group Inc., the insurance giant. Both firms have seen their stocks get hammered, and their managements spent the weekend trying to come up with plans to reassure the markets.

"Monday will be a day of reckoning for the financial markets," said Carlos Mendez, senior man- from some of its subsidiaries to the holding company.

Merrill, whose retail brokerage force is the largest in the country and is known as the "thundering herd," quietly engaged in discussions with Bank of America, whose retail bank branches stretch coast to coast. Wall Street executives said the Federal Reserve may be involved in orchestrating the sale, figur- major rivals on Sunday—the euro, the Swiss franc, the U.K. pound and the Japanese yen.

Some executives involved in the Lehman discussions held out hope that an 11th-hour reprieve would materialize. Under one scenario aimed at limiting the ripple effects of Lehman's demise, a group of about 15 banks were in discussions Sunday to pool about $100 billion, which would

Ultimatum By Paulson Sparked Frenzied End

Source: The Wall Street Journal

The Bottom Up

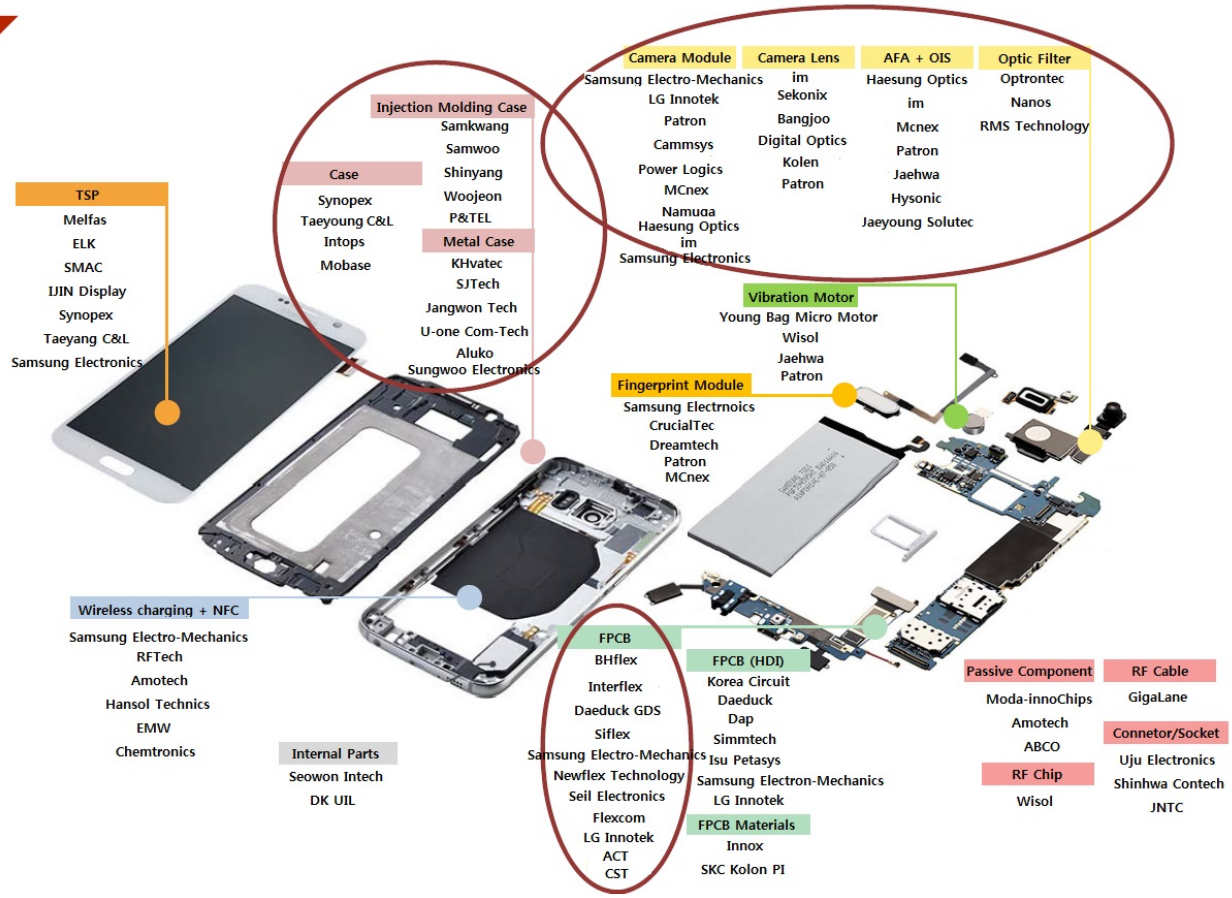
Over the past sixty days, Wall Street has turned on Apple, its once favorite technology stock. Last month it was Guggenheim, UBS, and Goldman Sachs. This week it was HSBC, cautioning on saturated iPhone markets and Rosenblatt Securities, which wrote that you would have to wait until 2020 to get paid again for owning Apple, coinciding with the 5G wireless upgrade cycle.

Pick a Model, Any Model

Source: Retiree News

Because every iPhone contains a bonanza of chips and other good stuff, those that make those components have also been taking it on the chin. This week it was Taiwanese lens maker Largan Precision, who reported an almost 30% fall off in year-over-year revenue.

The Parts Inside



Source: ITRS News

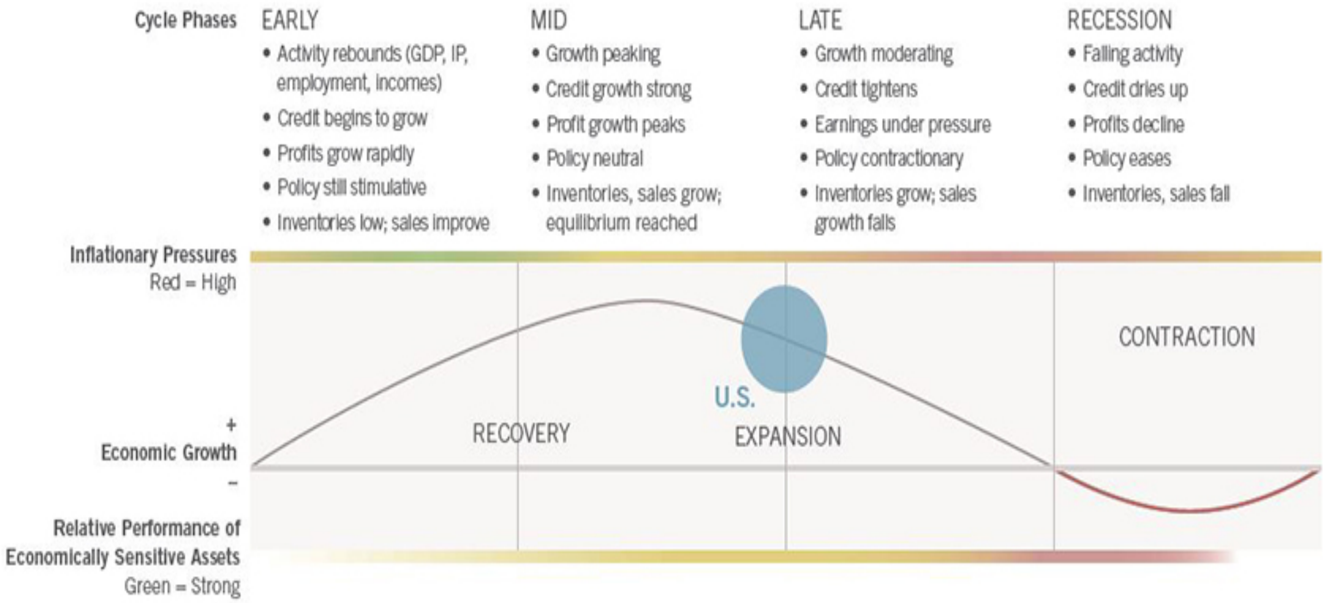
Morgan Stanley’s chief equity strategist, Mike Wilson, is the man with the hot market hand. Having called much of the rally in the last two years, his outlook isn’t that rosy going into 2019. As he accurately points out, we are in a rolling bear market that is hitting one sector after another. He expects high P/E growth stocks that don’t deliver to get “severely punished”.

Morgan Stanley’s Mike Wilson

Source: CNBC

Mike also makes a really good point about how frustrating this is going to be for bulls and bears. “As part of our rolling bear market theme, it’s going to be a very unsatisfying bear market to the bears. Why? Because you’re in a structural bull market. And when you’re in a structural bull market you don’t get the big earnings collapse.”

Sliding to the Right



Source: Fidelity Investments

Markets

Just when the global markets were in need of a sense of calm and stability, on Wednesday night they got neither.

Futures Fall Off the Table

Source: CNBC

This sudden high volume spike down in the futures market, is being attributed to a fund, or funds, that needed to liquidate or square off a big position. This type of liquidation, if that's what it was, can destabilize the markets and lead to a "bid wanted" situation.

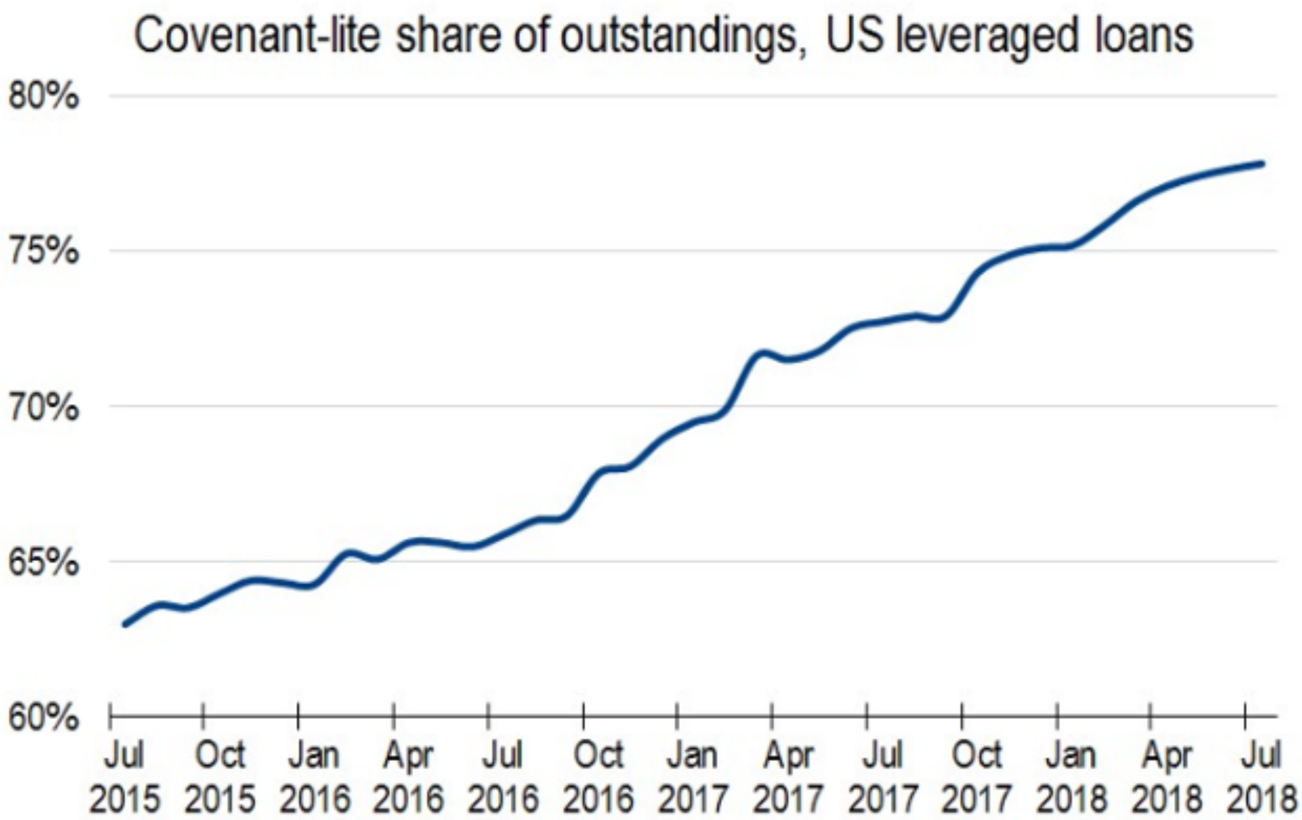
In an appearance on CNBC, Omega's Lee Cooperman, placed the blame on 'algorithmic, trend-following models'. While we love Lee and all he has accomplished, the playing field is now forever changed. And when these irrevocable things happen, 'don't hate the player, hate the game', as the hip kids like to say.

The Genie Is Out of the Bottle

Source: Fame Focus

When Apollo Global Management co-founder Leon Black talks, it's best to listen. This week at the Goldman Sachs Financial Services Conference he shared his opinion, that credit markets have become too frothy for comfort. In an interview Black said, "The credit markets, unlike the equity markets, have gone to bubble status. The amount of covenant-less debt is more than 2007. You have a thirst for yield that exists on a global basis. So there is true excess."

Risky Debt Floods the Market



Source: LCD

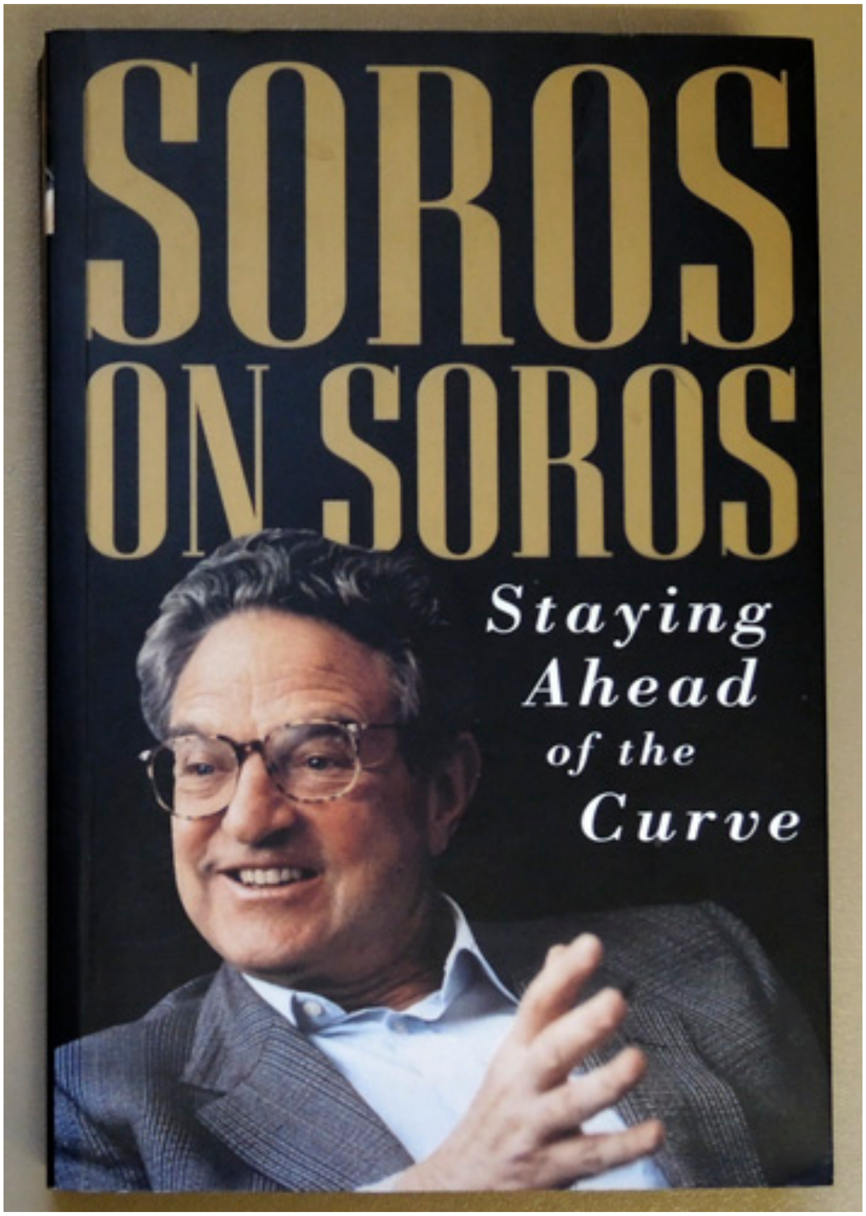
The high-yield market is also beginning to show some signs of stress, as junk status energy debt is being negatively impacted by the selloff in oil prices. Equities take the lead from credit spreads and tend to do well in a contracting environment and exist as the opposite when they widen. So far the move doesn't look like more than a blip on the radar. Having said that, every long journey begins with a few small steps.

Pump Baby Pump

Source: Oliver Wyman

All this fury and fear in the markets gives us the chance to re-visit George Soros' "Theory of Reflexivity". While there are more complicated ways of describing it, in it's basic form the theory makes the supposition that an objective reality exists, and over time it can be influenced by subjective perception. Eventually the latter takes over, and perception becomes reality. Soros originally proposed his theory in a book that anyone interested in understanding markets should read, "*Soros on Soros, Staying Ahead of the Curve.*"

The Good Book



Source: Bridgebook

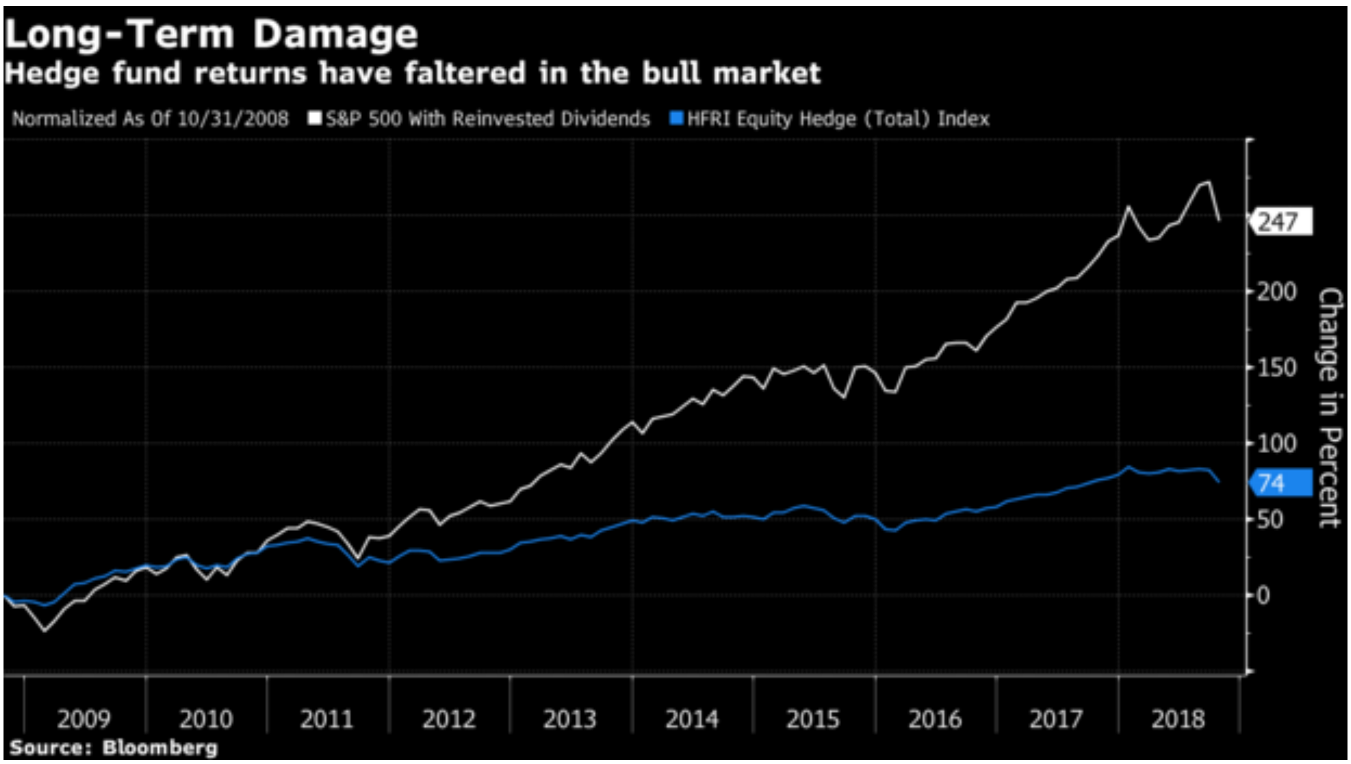
We brought reflexivity back to the table because there is currently a negative feedback loop developing. The building perception is that global growth is shutting down, profits have peaked, and a recession is on the horizon. This narrative could become reality, validating the downward pressure on markets and causing the consumer, and 70% of the economy, to exacerbate the situation by retrenching.

Hedge Funds

If you are actively employed in the hedge fund industry, or are considering doing so, this next section should be read with both caution and a Xanax, or a glass of Maccallan, at the ready. You have now been sufficiently warned. Read on at your own risk.

In news that is a far from breaking, *Bloomberg* reports that hedge funds are having another tough year, making it the seventh one in a row.

A Mississippi Sized Delta

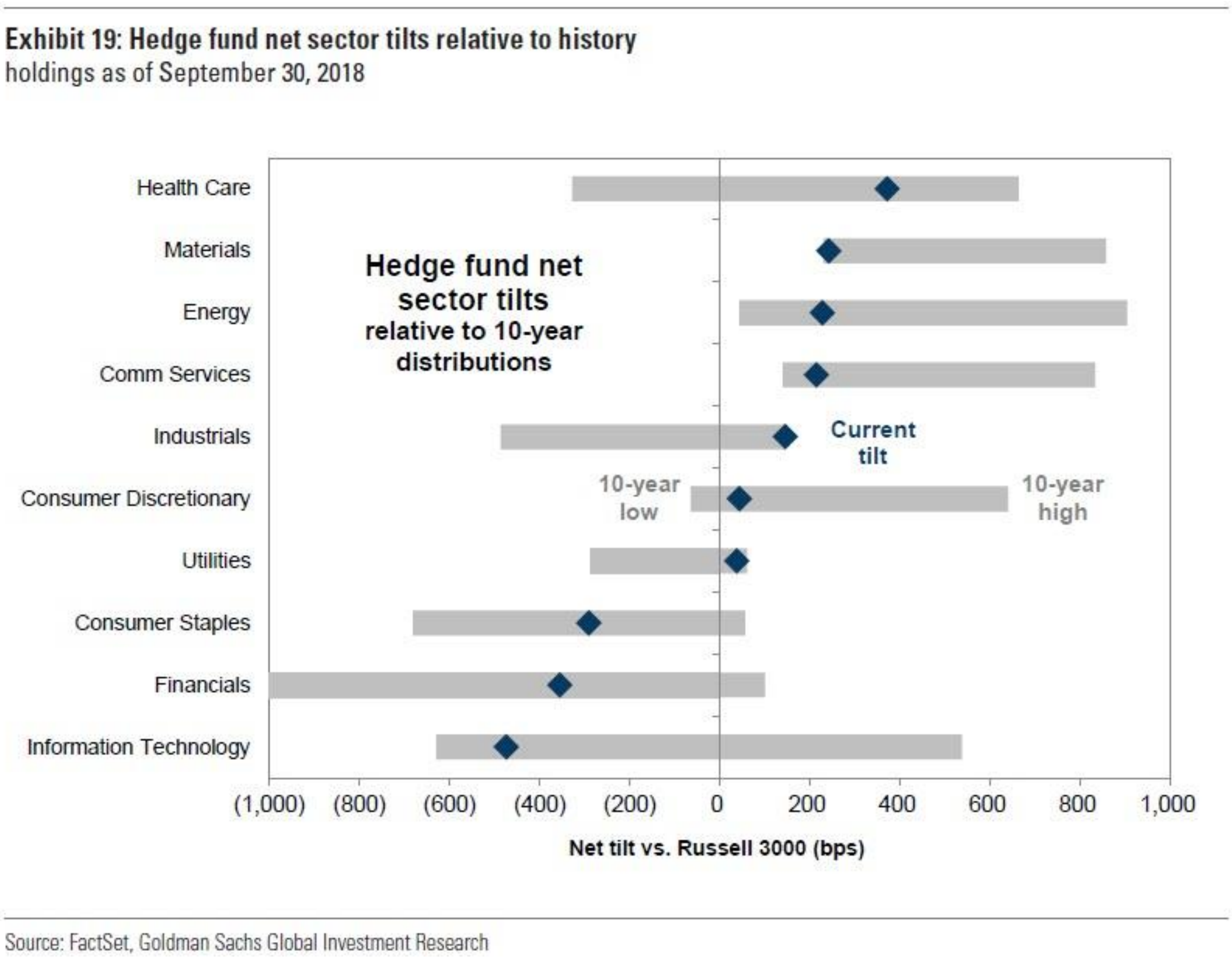


Source: Bloomberg

In defense of the industry, in straight up bull markets investors should be making most of their money by being long the cheapest exposure they can find. Whether it be the Russell 1000 Growth at 20 basis points, the S&P 500 at 5, or Fidelities' array of free ETFs, either way, you just wanted to be long.

Now here is the news that is not in defense of hedge funds. Just because you can run with a low net exposure, doesn't mean you always should. When the author was developing liquid alternative equity funds for Nuveen in 2008 and 2009 the charge was to provide consistent singles with low volatility. This perceived demand was born out of the damage done to investor psyche after the global financial crisis. Years later, that move proved ill placed as a low vol 3% is less appealing to the masses than a higher vol 10%, and now we are dealing with the consequences.

Which Way Managers are Leaning



Source: Goldman Sachs

November was particularly cruel to even the biggest and most established managers. *Bloomberg* reports that Citadel was down 3%, the worst monthly performance since 2016. Steve Cohen's Point 72 lost 5%, wiping out this year's gains, and Izzy Englander's Millennium fund, one of the most consistently posotive in the industry, was down 2.8%, the third worst month on record. Smaller funds like Brenham Capital Management, an $800 million energy focused fund, are also shutting down.

Englander, Griffin, and Cohen

Source: Bloomberg

For any analyst, portfolio manager, or marketeer of hedge funds who is feeling alone in a changed world, you have company in the form of David Goldberg. Turns out Dave is like a growing number of 45 to 55 year old journeymen employed in the alternatives craft that could not find a way to stay in the game. After two years without a paycheck, he settled on picking cannabis stocks for Merida Capital Partners in Manhattan. “Smoke em’, err eat em’ if you got em’.”

Picking Ganja and Gummies

Source: Review Journal

Diversions

Unless you are a delusional Georgia Bulldog fan, the NCAA selection committee got it right by putting the one-loss Oklahoma Sooners in the finals with undefeated Clemson, Alabama, and Notre Dame. From the way the teams have been playing, it's Clemson's or Alabama's to lose. *ESPN* ranks every bowl game by "entertainment value", including the Bad Boys Mowers Gasparilla Bowl.

It's too bad that the NCAA replaced the iconic Waterford Crystal championship trophy with what looks like a piece of bronze scrap metal. An added bonus was that it was very entertaining to learn about the many ways the ball broke over the years. A younger Nick Saban holds the 2012 trophy, it too didn't make it.

Shiny Object, Shiny Object!

Source: Champions Club

Like most of America, we took time Wednesday to reflect on a kinder and gentler period in our political history. Hearing the stories about how Bush 41 lived his life and treated others was a nice reminder of that time. I managed to hold it together for the most part, that is until 43 told the world how lucky a son he was to have a dad like his.

George W Bush Says Goodbye

Source: The New York Times

There was plenty to recount about George Bush's life this week, much of which was widely covered. Here are a few of the smaller things that might have fallen off the radar.

The Union Pacific train that took Bush to his final resting place in College Station, Texas, Bush 4141, was one that he was familiar with. Commissioned in 2005, the former president got a chance to drive it once, saying to the engineers aboard, 'Can I take this out for a drive? Can I run it?' It would have been rude to say no.

Union Pacific's Bush 4141

Source: Union Pacific

After college, and serving in the Navy in World War II, George left an upper crust life in New England for the tough oil fields out west. The family quickly learned that the life of a drilling equipment salesman was going to have many stops.

Two of those were here in California. In 1949 Barbara and George moved to Bakersfield. It's there 'W' spent his third birthday. The home at 2101 Monterey Street is now owned by political consultant Mark Abernathy and the plan is to convert it into a museum and learning center to help teach Spanish speaking children English.

A Very Young 'W"

Source: ABC News

Bakersfield wasn't the two future presidents only home in the Southern California. They also resided in Compton for a short period of time. This was the last place they stopped before heading to Midland.

Other notable residents of the city were Eddie Murphy, Snoop Dog, Ice-T, Ozzie Smith, and Kevin Costner. Tupac Shakur was ironically never ‘straight outta Compton’. Instead, he went to Mount Tamalpais High School in Marin County.

With that, we turn the page on a memorable week, both inside and outside of the markets. We wish everyone the best as we enter the final month of the year. We also wish our past president Godspeed and hope that he, Ronnie, Barbara and Nancy are all getting a good laugh out of things down here.

Bush & Reagan…Together Again

Source: Politico

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