

Stillwater Capital - This Week in the Markets



The Top- Down

It was a quiet week from the top-down with most of the market making news coming from outside the world of finance.

The proposed June 12th meeting between President Trump and Kim Jong-un may now be off due to a fight over nukes. The president believes that Chinese President Xi Jinping's influence could be the catalyst that caused North Korea to threaten to pull out from the negotiations.

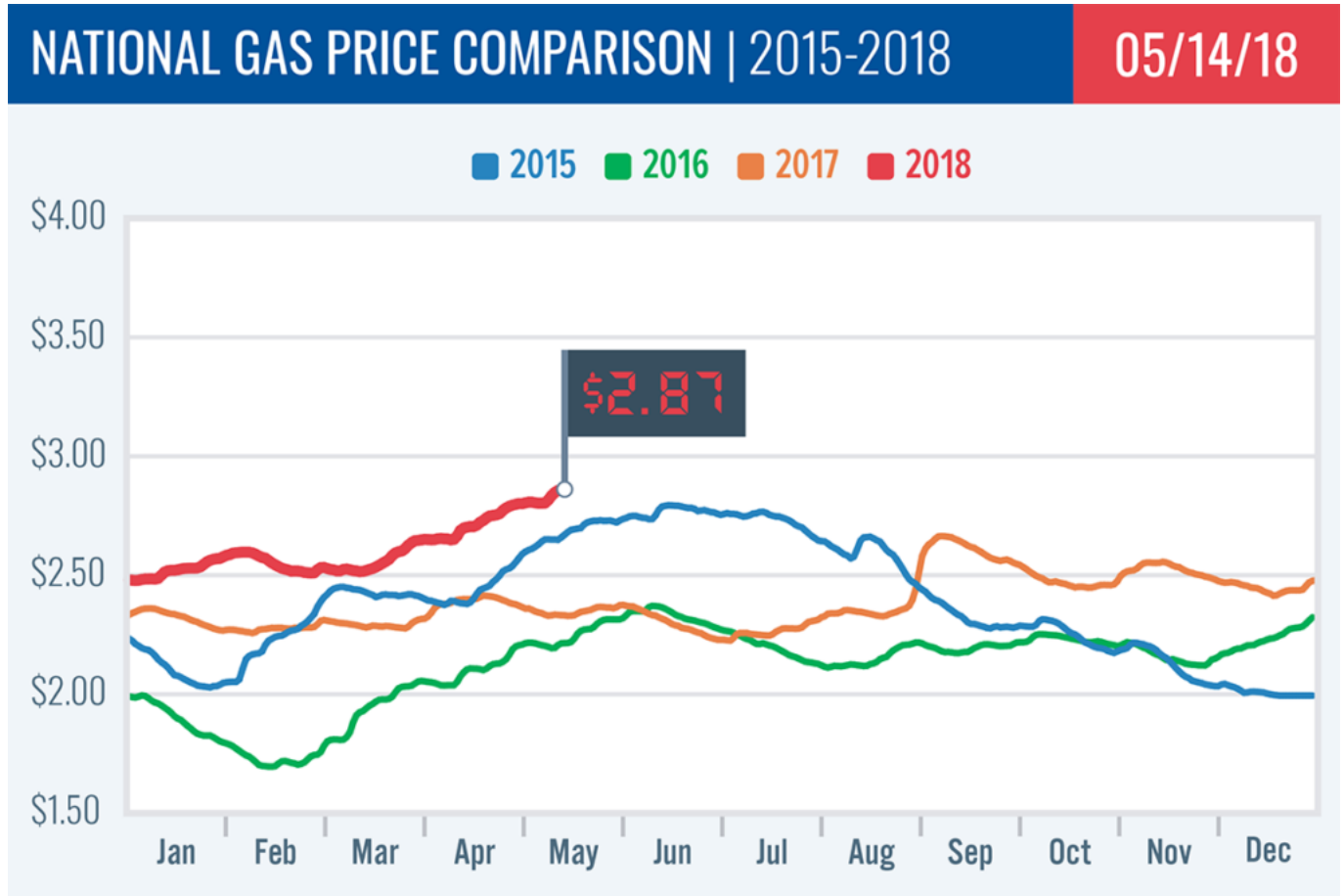
Kim Jong-un & Xi Jinping



Source: Business Insider

Tensions and violence are increasing in the Middle East , following the decisions by the US to withdraw from the landmark 2015 Iran nuclear deal earlier this month. This event is equally responsible for pushing oil prices above \$70, with the summer driving season fast approaching.

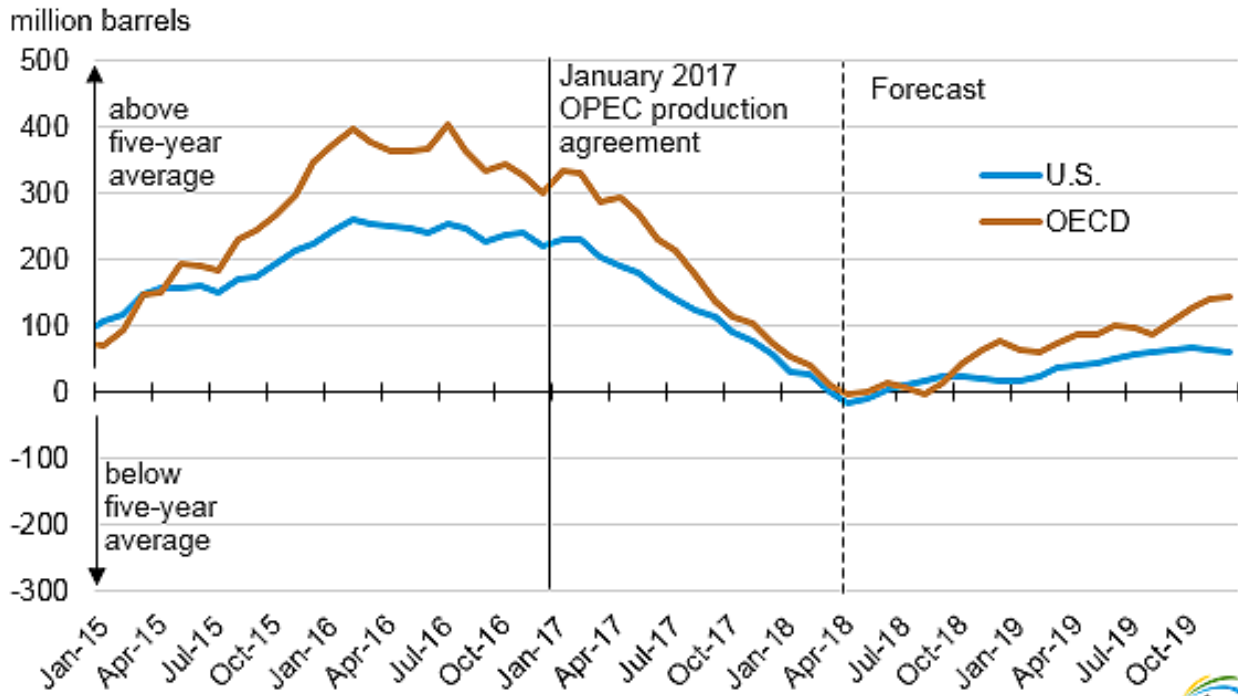
Gas Prices in 2018



Source: AAA

Meanwhile crude oil and finished product inventories have fallen below their five year average. Further supporting the current price.

Crude Oil & Finished Product Inventories

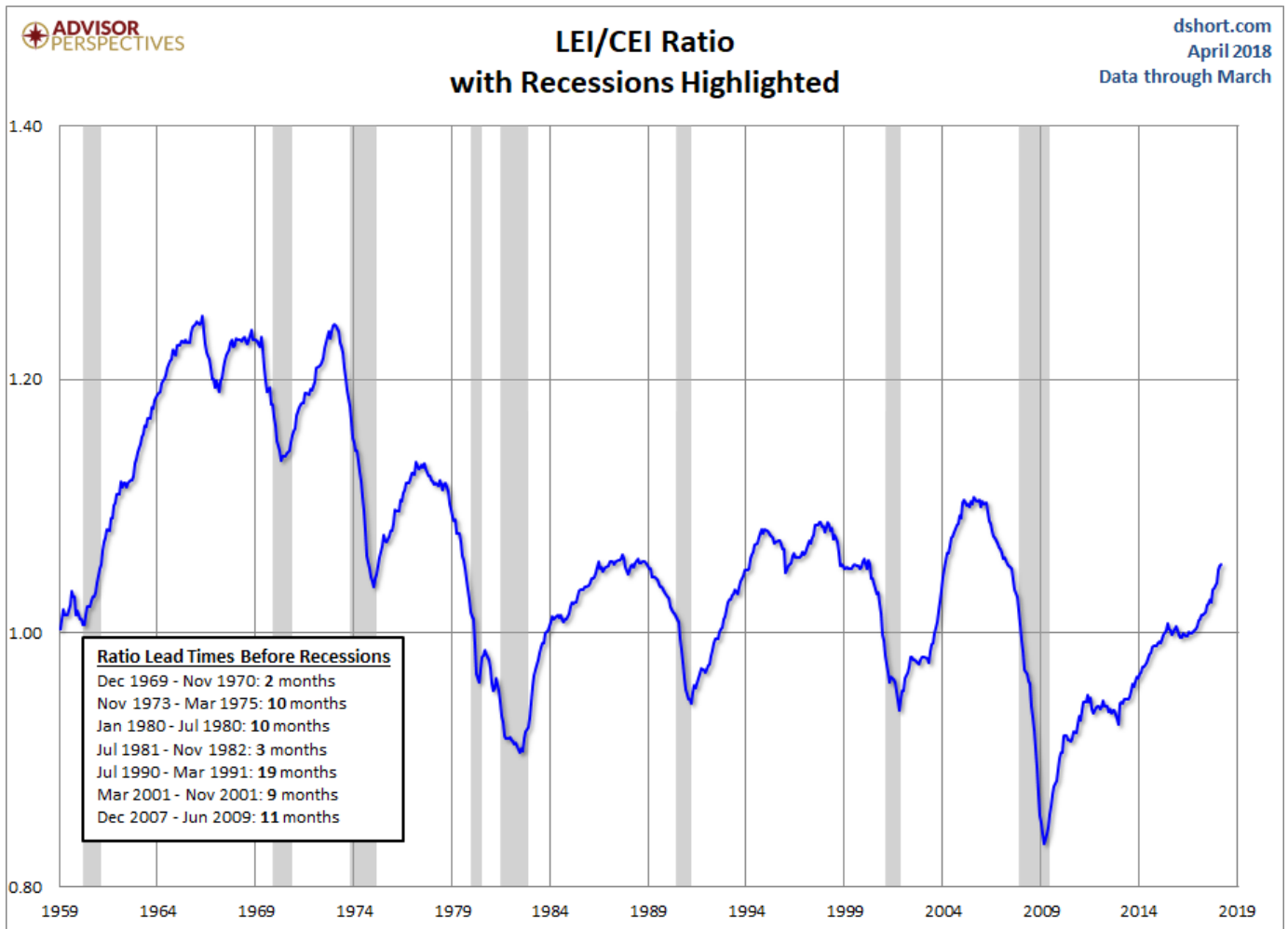


Source: EIA

Stillwater View: Still bullish on energy as the backdrop favors higher crude prices. A late cycle rally above \$100 is looking more and more like a real possibility.

In economic news here at home, Leading Economic Indicators continue to show smooth sailing ahead, with a 0.4% rise in April, marking the sixth straight monthly advance. Historically, The US economy has never gone into recession when LEI was headed higher.

Leading Economic Indicators



Source: Advisor Perspective

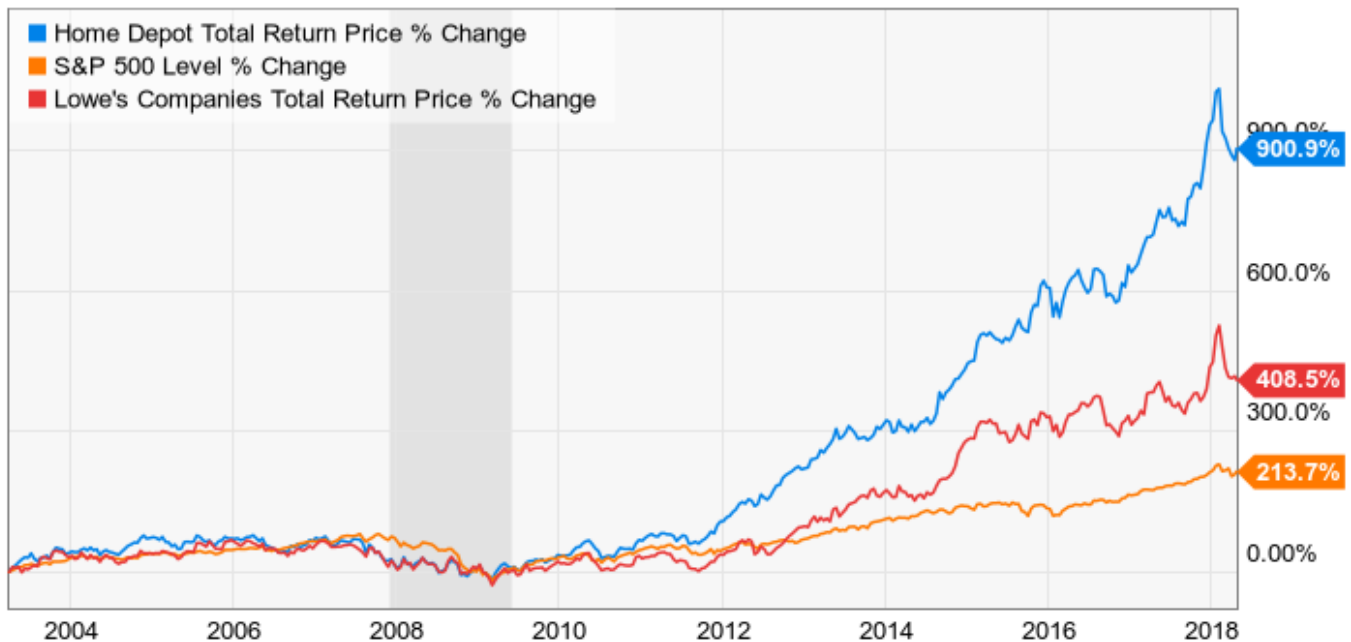
Stillwater View: At this point, there is little in the way of negative near term economic news to upset the apple cart. Employment, Leading Indicators, ISM, and even inflation are all signaling the green light for solid growth ahead in 2018.

The continued cooperation of interest rates and earnings, is something that remains to be determined. The market's favorite gadfly, Jim Cramer, thinks that the Fed and its plan for higher rates is the only thing that can get in the way.

The Bottom-Up Focus on Housing

The Home Depot gave investors something to think about this week when it reported earnings below what the Street expected. Market observers were quick to draw the conclusion that this showed signs of a housing market beginning to cool. The company blamed it on a spring 2018 bear market in gardening.

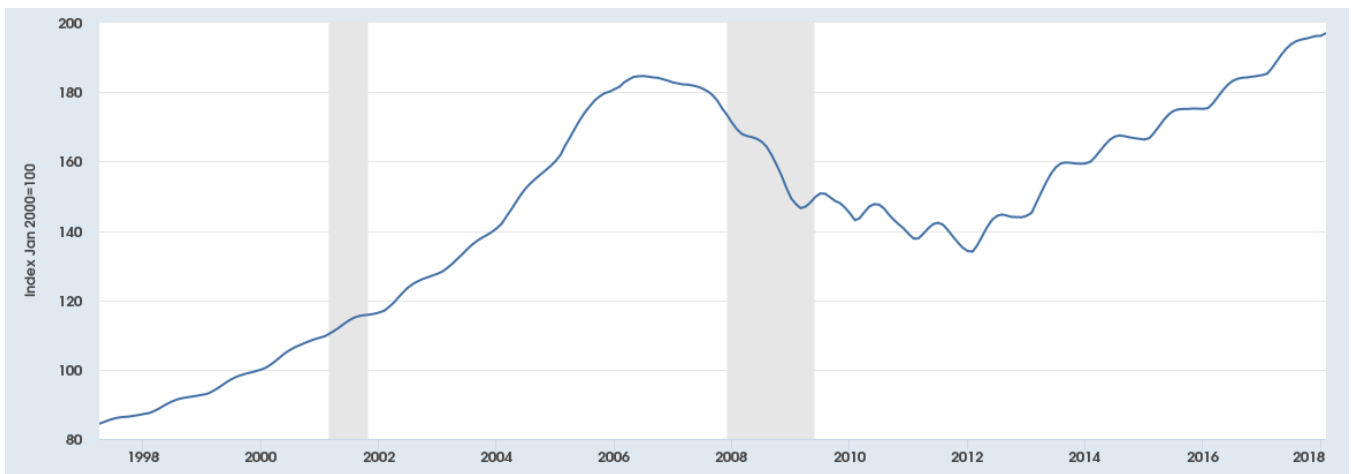
Home Depot, Lowe's vs. S&P 500



Source: Nasdaq & the Motley Fool

With home prices up dramatically from their post recession lows in 2012, market participants are watching with keen interest for any cracks in the foundation of an otherwise very strong housing market.

Case-Shiller 20-City Home Price Composite



Source: The Saint Louis Federal Reserve

With interest rates on the upswing, it's hard not to question how much longer this uptrend will remain in place. CNBC reports how rates for prime borrowers are surging this year to a 7 year high.

To keep this in perspective, rates bottomed out at 3.5% in the summer of 2016, but were running in the 6% range just prior to the 2008-2009 recession.

30-Year Fixed Mortgage Rates Moving Higher

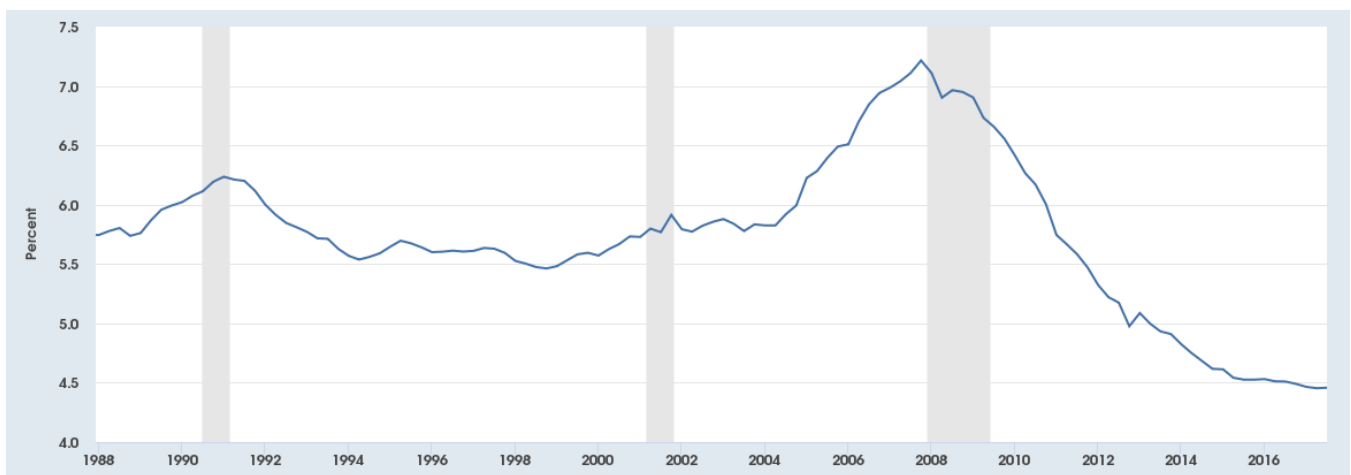


Source: St. Louis Federal Reserve

Home prices have benefits

Meanwhile, Wall Street is back at it, bundling riskier and riskier bonds into nice clean packages for yield starved investors. This being said, even the biggest housing bear must admit the system is far less levered than it was going into the Great Recession, as debt to mortgage service ratios are well below the 20-year trend.

Mortgage Debt Service as a Percentage of Income



Source: St. Louis Fed

Stillwater View: Let's boil this down to the simple fact that while home price appreciation is and always will be a key contributor to household wealth, when the tide went out last time, a mountain of wealth was destroyed with many being stopped out at the bottom by foreclosure.

Fast forward to today, the Bernanke led Fed declared war on asset price depreciation with its zero interest rate policy (ZIRP). Given the state of the economy today, and if you owned assets (stocks, real estate, private companies), chances are strong you have been reflat.

In other words, beware when you observe changes at the margin and an incredibly accommodative interest rate environment becomes less so each and every day.

Stillwater "Fat Pitch" Strategies

With our focus on alternative equity solutions, Stillwater is always on the lookout for fat pitches in the market. These are opportunities where the risk/reward of a sector or theme is skewed heavily in our favor.

We use basic math, stating that if we feel there is less than 20% downside and greater than 50% upside over the next 12 to 24 months, it's a fat pitch. Earlier this year, we made the call declaring the very underappreciated energy sector was due for a comeback while the upside/downside skew was favorable. So far this view has been rewarded.

Schlumberger, EOG Resources, Phillips 66 vs. S&P 500



Source: Nasdaq

Today we are putting together a basket of housing, mortgage and real estate related securities that will benefit our investors in a cooling of the overall market. While we aren't predicating a 2008 type of washout, with rates on the rise and the economy showing strong signs we are arriving late into the cycle, now is the time to prepare for the opportunity.

Sprawl Happens



Source: The Vancouver Star

Just like Ted Williams, the last man to hit above .400, waiting on those fat pitches can have a profound impact on your batting average.

Ted “Teddy Ballgame” Williams



Source: MLB

Up & Down Wall Street

Bloomberg reports that JP Morgan is going mainstream, offering access to previously exclusive alternative investment pools for the \$100,000 client, containing strategies include private equity, real estate and hedge funds.

Anton Pil, managing partner of JP Morgan global alternatives had this to say about the announcement: “Many high-net-worth investors continue to be under-allocated to alternatives relative to their institutional counterparts. As we get later in the economic cycle, identifying alternative sources of return is an essential consideration for investors looking to build stronger portfolios.”

Core Equity & Fixed Income with Alternative Satellites

Alternative Investments

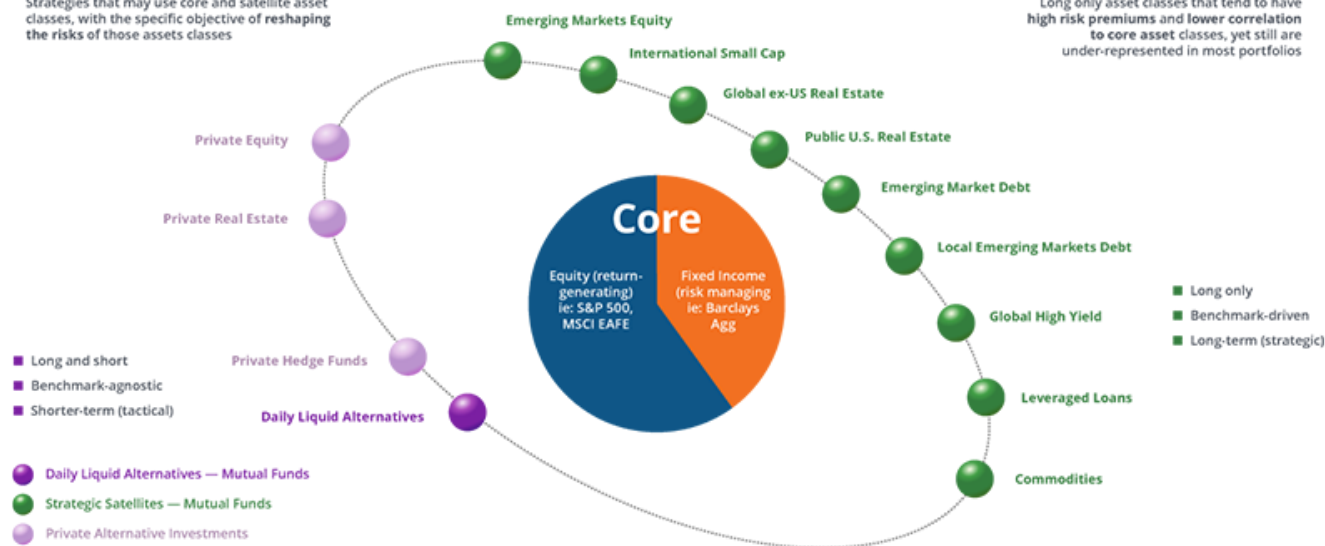
Risk Re-Shapers

Strategies that may use core and satellite asset classes, with the specific objective of reshaping the risks of those asset classes

Strategic Satellites

Return Enhancers

Long only asset classes that tend to have high risk premiums and lower correlation to core asset classes, yet still are under-represented in most portfolios



Source: Brazos Capital

Stillwater View: While we would hate to be accused of talking our book, in this case we indeed are, and for good reason. When you get into the late cycle of the economy and market, alternatives begin to look a lot more compelling. They can help take risk off the table and enhance downside protection when the economy eventually runs out of room.

Stillwater Alternative Equity strategies start off with a \$100,000 minimum investment and provide flat pricing of 1%, daily liquidity, and transparency of holdings. A great option when the equivalent private fund usually costs 2% of assets and 20% of profits while locking up your money for a year or more. We welcome all inquiries.

All asset management firms with over \$100 million are required to report their holdings to the SEC in a document called a 13F filing. This week, those were made public as part of the regular course of business.

And when they are, the business media breathlessly reports which managers are making what moves and whether or not it shifts and influences the market. Best quote we have seen to describe the situation comes from Barron's. Writing, "Warren Buffett and his quarterly changes to his portfolio are to Wall Street as Gigi Hadid and what she is wearing are to the glitterati."

Montecito Native Gigi Hadid



Source: Metro UK

And with that, here is Stillwater’s attempt to report all the news that has been previously reported...

MarketWatch has the “20 stocks that hedge funds love most”. CNBC reports much the same when they cover “The top performing stocks that hedge funds are buying – including Chipotle”. Meanwhile Bloomberg covers the story of how Fidelity and Bridgewater have found value in steel maker Cleveland Cliffs on the back of the tariffs imposed by the White House. ValueWalk provides the best Q1 2018 snapshot of moves we have found of interest so far this quarter.

Stillwater View: At the end of the day, these moves by the “smart money” have become less and less relevant as time goes on. Fewer funds have adopted true alpha generating strategies in recent years, and therefore the news of what they are doing is starting to fall on deaf ears, as much as we would like to report otherwise.

First Quarter 2018 Performance of the Major Hedge Funds

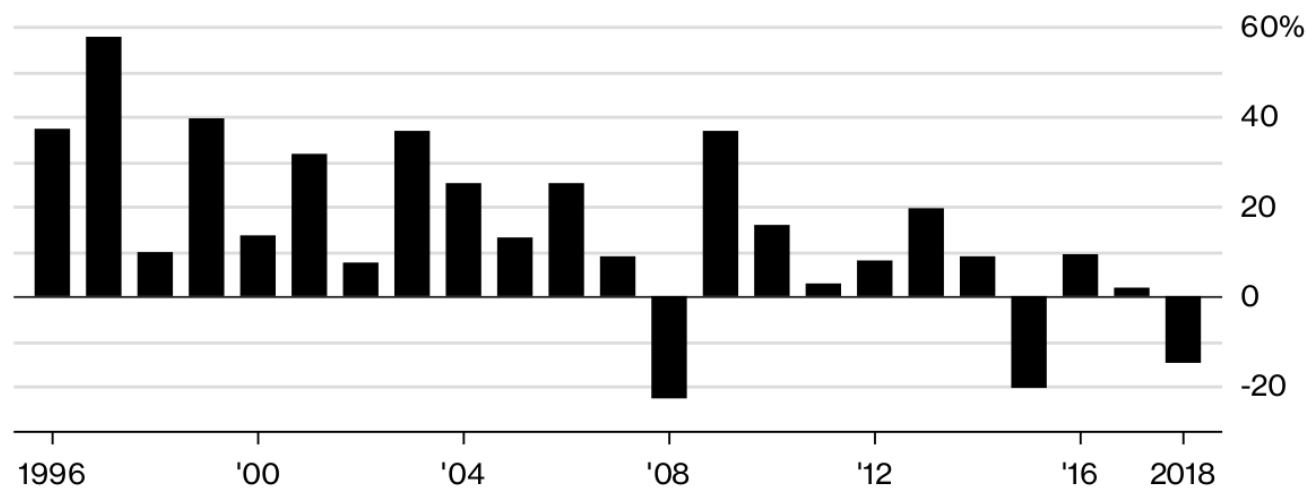
Odey European	12
Voce Catalyst Partners	7.9

Tiger Global Management	6.7
Marshall Wace Eureka	4.1
Citadel Global Equities	2.1
Viking Global Investors	(0.2)
Glenview Capital Management	(7)
Pershing Square	(8.6)
Greenlight Capital	(14)

Source: Bloomberg

We almost feel bad by continuing to include stories that highlight the challenges David Einhorn and Greenlight Capital are facing. But we do it with Elon Musk and Tesla, so we might as well be consistent. This week Bloomberg reported the established notion that Einhorn is having what many would call a “hedge-fund midlife crisis”.

Greenlight’s Performance Through April 2018



Source: Bloomberg

Diversions

The literary world wept this week as iconic writer Tom Wolfe passed away at the age of 88. Wolfe was part of the New Journalism movement, a writing style that involved deep immersion into the

subject matter for the author. The genre included the likes Truman Capote, Joan Didion, Hunter S. Thompson, Norman Mailer and George Plimpton.

Tom Wolfe



Source: The New Yorker

Stillwater View: Goodbye and Godspeed to the man who made the white suit so very well..

The 107th Bay to Breakers will take place this Sunday, and many residents of San Francisco are doing what they do best during the spring ritual race, and that is to cope. The run itself isn't much of a race to the finish. It starts off in in the financial district, takes runners up Potrero Hill, and then culminates in Golden Gate Park.

Long Live the Centipede



Source: Runners World circa 1984

Stillwater View: Having participated, I can say with reasonable authority that it is a hell of a lot of fun along the way.

Chicago's skyline may be changing forever if the plans unveiled this week by Related Midwest become a reality. The company gave the public their first look at what the city can expect if plans go through for their dual towers on shores of Lake Michigan.

400 Lake Shore Drive



Source: Chicago Tribune

To some, this is far more palpable than the original Santiago Calatrava designed Chicago Spire that was put to architectural rest in 2014.

The Chicago Spire



Source: Arch Daily

All that is left from the original effort is a round hole in the ground that was supposed to be the footing for the long-languishing site. It has sat abandoned since 2008.

The Abandoned Chicago Spire Footing



Source: Chicago Tribune

To subscribe or unsubscribe to Stillwater Capital's "This Week in the Markets" please e-mail contact@stillcap.com.

DISCLOSURE: Stillwater Capital, LLC is a Registered Investment Adviser. Advisory services are only offered to clients or prospective clients where Stillwater Capital, LLC and its representatives are properly licensed or exempt from licensure. This website is solely for informational purposes. Past performance is no guarantee of future returns. Investing involves risk and possible loss of principal capital. No advice may be rendered by Stillwater Capital, LLC unless a client service agreement is in place.

Stillwater Capital, LLC provides links for your convenience to websites produced by other providers or industry related material. Accessing websites through links directs you away from our website. Stillwater Capital, LLC is not responsible for errors or omissions in the material on third party websites, and does not necessarily approve of or endorse the information provided. Users who gain access to third party websites may be subject to the copyright and other restrictions on use imposed by those providers and assume responsibility and risk from use of those websites.

General Notice to Users: While we appreciate your comments and feedback, please be aware that any form of testimony from current or past clients about their experience with our firm on our website

or social media platforms is strictly forbidden under current securities laws.