



The Top-Down

On Wednesday, the S&P 500 closed 0.6% lower, ending a streak of 50 consecutive days without a decline of 0.5% or more. The longest since 1965. Barring a major correction today the index will mark a run of 62 consecutive weeks without moving lower by 2%. A record also set back in 1965. For the last year and a half every dip below the 50-day moving was an opportunity to buy if you wanted long exposure.

S&P 500



Source: Nasdaq

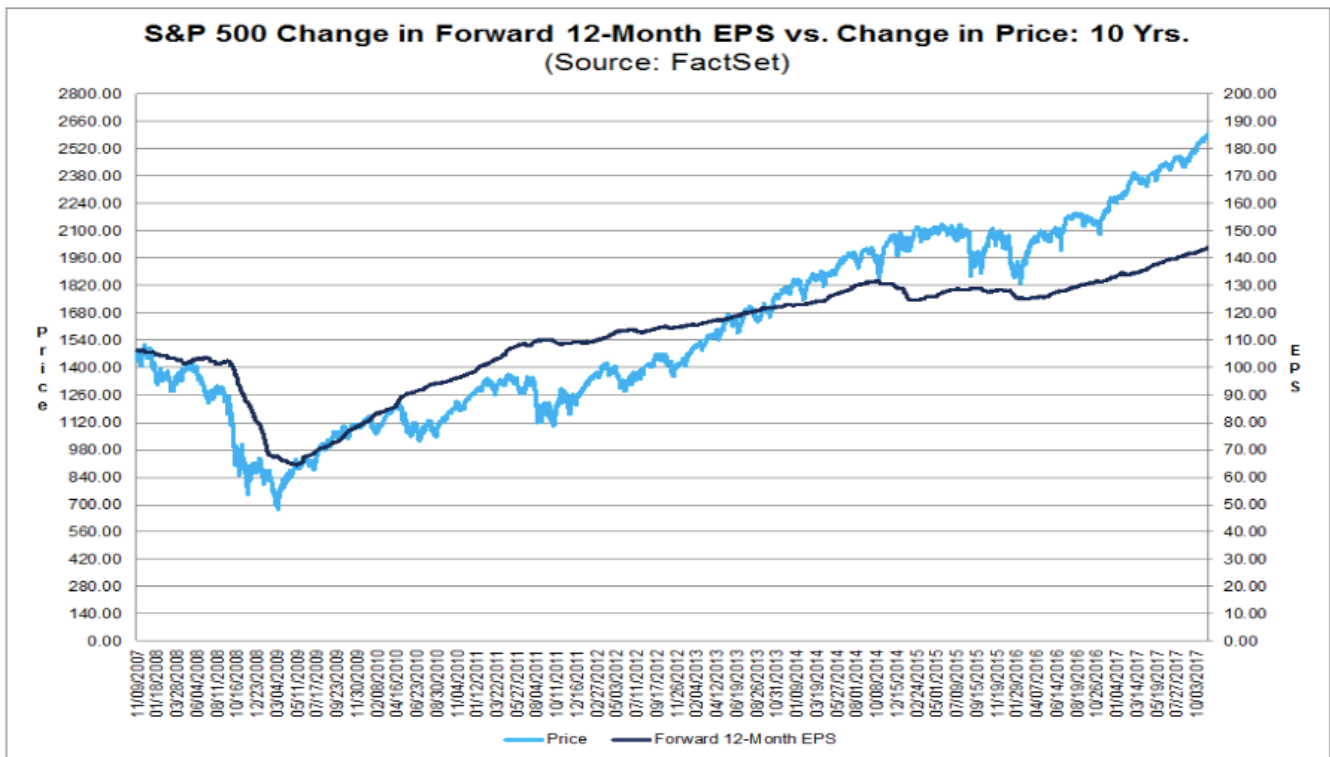
Stillwater View: It happened, it finally happened. A 0.6% ‘correction’ in the S&P 500. Bigfoot, The Tooth Fairy and the Easter Bunny are now back on the table.

Gary Cohn went out this week to sell corporations on the business benefits the GOP tax plan could provide. What he heard back in exchange was crickets. When the audience at the *Wall Street Journal* sponsored CEO Council summit were asked if they planned to increase capital investment

few in the audience raised their hands. This prompted Mr. Cohn to ask awkwardly, ‘Where are all the other hands?’ Treasury Secretary Mnuchin made an appearance on CNBC today, saying that he expects a tax bill on the president’s desk by Christmas.

Stillwater View: Prepare yourself now for the long public debate on the benefits of the tax plan, assuming it includes permanent cuts to corporate rates. C-Suite executives have learned to run leaner operations following the global financial crisis. That shows up in the record earnings that continue to drive the market higher.

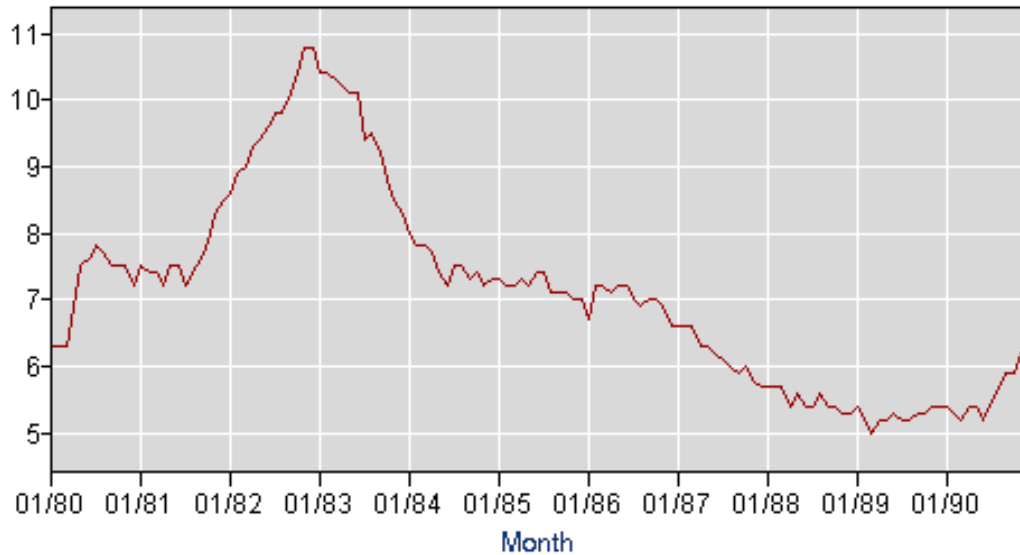
S&P 500 Earnings and Index Performance



As Wall Street discounts the potential economic boost from tax-reform, it’s beneficial to look back at the conditions that existed when President Reagan signed the Economic Recovery Tax Act of 1981 and the Tax Reform Act of 1986 into law.

In 1981, unemployment was still on the rise as we entered recession. Five years later it was descending, though still at 7%. A level much higher than the market considers to be full employment. *The Washington Post* provided historical context and a checking of the White House facts giving tax cuts get full credit for the above average growth experienced the rest of the decade.

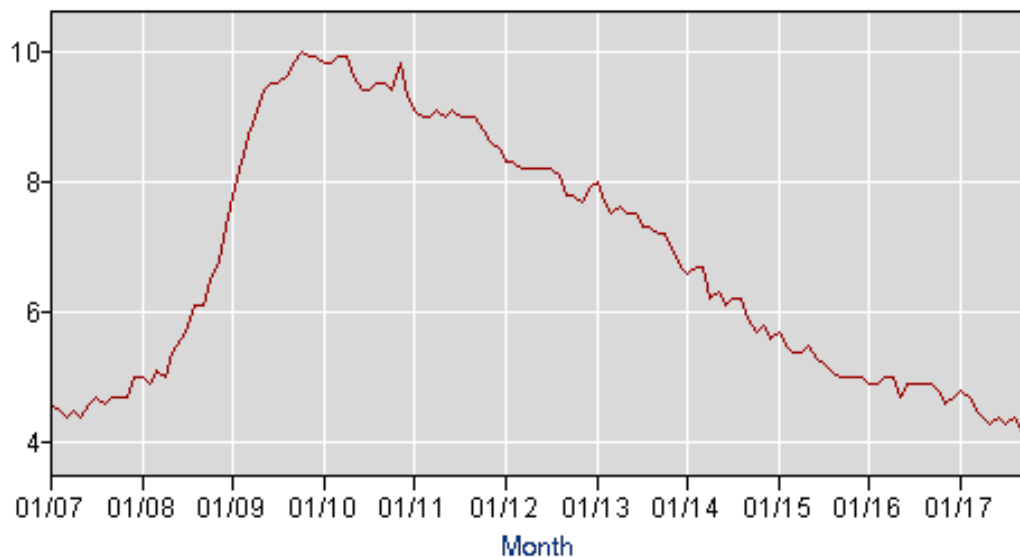
The United States Unemployment Rate From 1980 to 1990



Source: Bureau of Labor Statistics

Fast forward to today, and unemployment is running at 4%. A full 3% less than in 1986. Goldman’s Lloyd Blankfein is worried that this is not the best timing for a tax cut, as the economy has momentum and stimulus runs the risk of bringing on inflation. Morgan Stanley’s CEO, James Gorman, thinks corporate rates in the US should be in the 20% range to be more competitive with the rest of the world. In his opinion, a move to that lower level would be “a very positive thing and stimulating for the economy.”

United States Unemployment Rate from 2007 to 2017

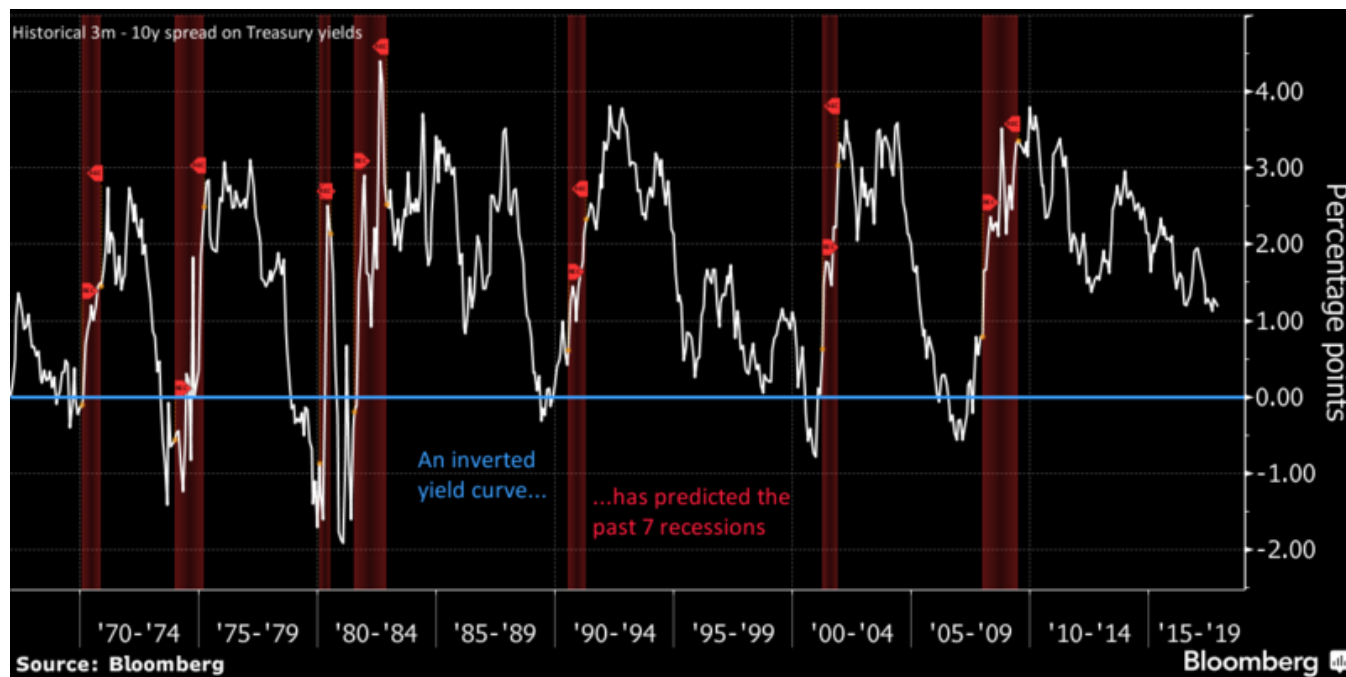


Source: Bureau of Labor Statistics

Stillwater View: Presidents inherit a set of economic circumstances when they take office and navigate them according to their own mandate, perceived or otherwise. President Trump is no different. The economy has recovered from the global financial crisis and a new set of risks exist. But for now, “laissez le bon temps rouler” as the French would say.

Credit markets continued to be the focus this week, as markets quickly turned their attention from junk spreads to a flattening yield curve. The latter serving as a sign that an economy which has shown little indication of slowing, might indeed be moving in that direction. BlackRock’s Russ Koesterich explains why it’s happening and if the market should be concerned.

An Inverted Yield Curve Predicted the Last Seven Recessions



Source: Bloomberg

Stillwater View: We have 100 basis points to go before the curve inverts. The equity markets will not respond well when it happens. The upshot for those long the market is that it could take a while to get there.

The high-yield scare lasted for just two trading sessions as the market quickly interpreted it was sector specific. So far, contained only to telecommunications.

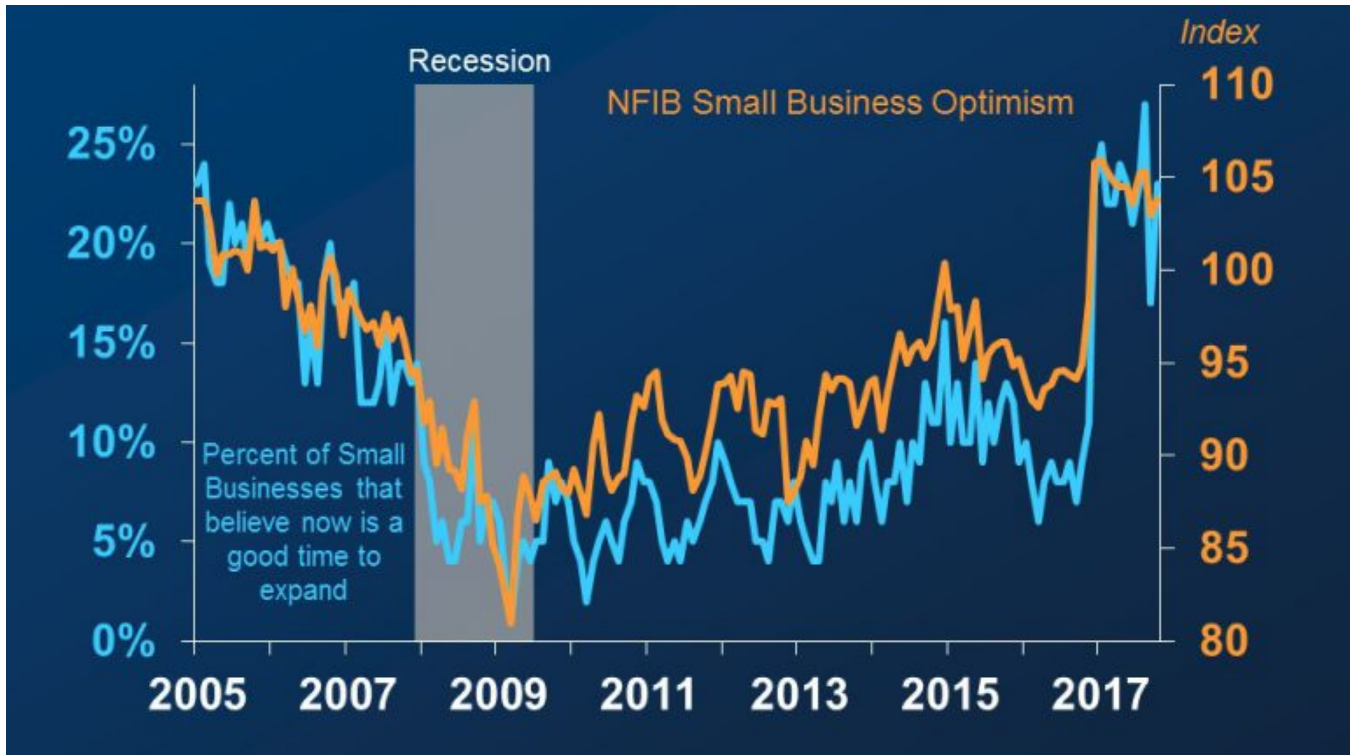
Telecom Debt Yields



Source: WSJ

The National Federation of Independent Business released their October small business sentiment index on Tuesday, showing a continued plateau that largely mirrors the return of the banking sector. Both saw a strong bump following last year's election yet have flat-lined for most of the year.

Small Business Optimism Index



Source: NFIB & American Banker Association

Stillwater View: Small business confidence remains an economic tailwind. Interestingly, it was falling in 2007 when the markets were hitting new highs. At that time, the domestic and global economy was firing on all cylinders.

United States Industrial Production – Back to New Highs



Source: The St. Louis Federal Reserve

The Bottom-Up

General Electric reduced their dividend for the first time since the Great Depression as cash flow concerns and weak growth have finally come home to roost. J.P. Morgan believes that even the reduced payout might be at risk.



Wal-Mart provided further proof that the consumer was on stable footing, as the most dominant presence in big-box retail reported strong revenue, earnings, and same store sales which have increased for the 13th straight quarter. The performance of the two biggest names in the business are on divergent paths.

Wal-Mart vs. Target Stock Performance – A Perfect Pair



Source: Bloomberg

Cable giant John Malone made ominous comments about Jeff Bezos and Amazon this week when he said the company is a 'Death Star' moving in 'striking range of every industry on the planet'. Consumer staple and food companies sold off on Wednesday, following news that the company was lowering prices at the recently acquired Whole Foods.

Stillwater View: Those looking for 'safer' and less economically sensitive sectors are having to rethink where they allocate assets, present company included. The race to lower margins is on and Amazon is in the driver's seat.

Jeff Bezos is at the Doorstep



Source: Slate

Buffalo Wild Wings received an unsolicited bid from Roark Capital to be taken private for \$150 per share. Roark had previously bought and sold an interest in competitor Wing Stop. Activist investor Marcato had been pressuring for change at BWW, grabbing three board seats and pushing out the previous CEO.

Buffalo Wild Wings



Source: Nasdaq

Mall REITs have not only stopped going down, many are up double digits this month as deals are being both rumored and announced. This had been an almost perfect one way short trade until early November.

Taubman Centers



Source: Nasdaq

In another confounding move, office REIT Vornado is up marginally after recently hitting a 52-week low. It's risk on for class-B and risk off for class-A. Opportunities abound and the frustration of trying to make a buck in REITs this year continues.

Vornado Realty



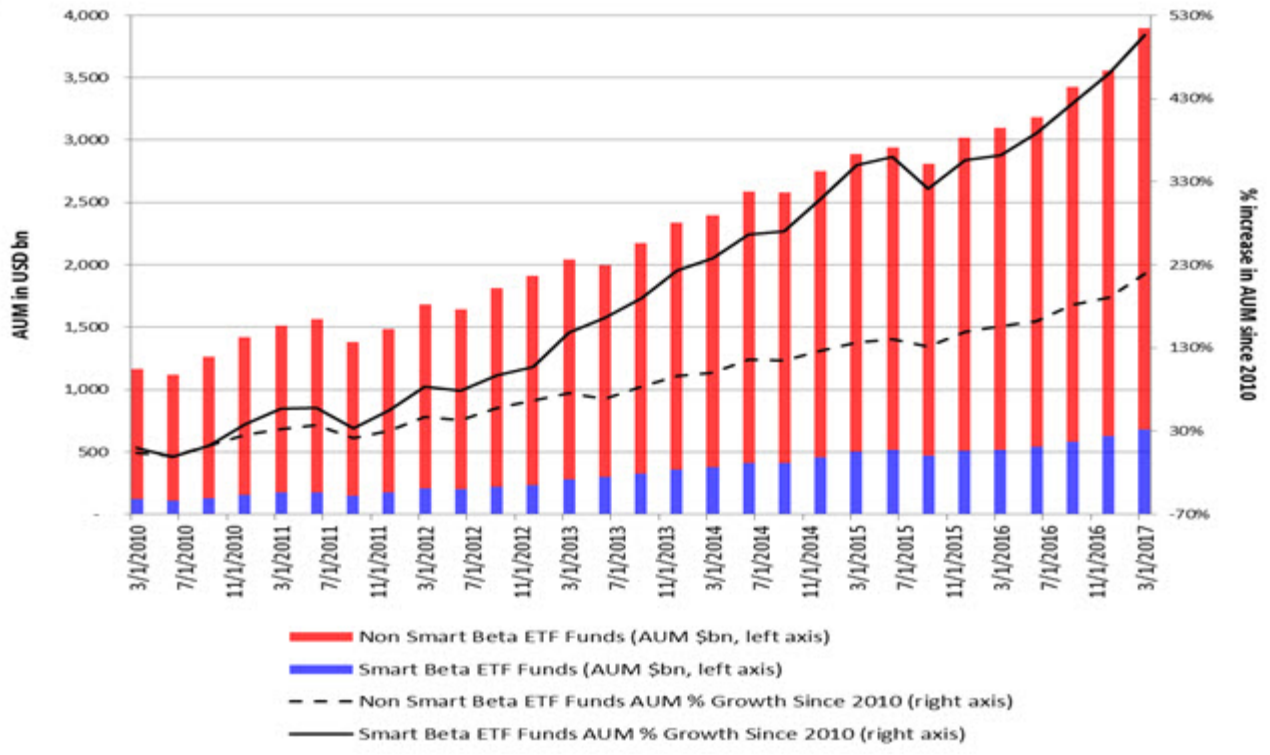
Source: Nasdaq

Up and Down Wall Street

Stillwater clears the ‘Up and Down Wall Street’ decks this week to focus on AQR Capital founder Cliff Ansens and the work he has done on the momentum factor and the application of it into AQR funds.

By way of background, Cliff was a student of Nobel Prize Winning economist Gene Fama at the University of Chicago. Gene, and his partner at Princeton, Ken French, did pioneering research on factor based investing. The Fama/French 5 Factor model was the foundation from which Smart Beta was built. Rob Arnott, founder of Research Affiliates, wrote a thoughtful piece last year analyzing “How Can ‘Smart Beta’ Go Horribly Wrong”.

Growth in Traditional and Smart Beta ETFs



Source: Wells Fargo “Quantitative Investing and the Rise of Smart Beta”

Momentum investing is exactly what it sounds like, on the long side it’s buying stocks that have shown a pattern of appreciation, and on the short side, a pattern of depreciation. But like everything, it’s not that simple.

In September 2014, AQR published a seminal paper for the *Journal of Portfolio Management* entitled “Fact, Fiction and Momentum Investing.” In it they refute certain myths, such as the data doesn’t go back far enough, and that it’s really only a game of ‘hot potato’. Momentum as a factor works. And as evidenced below, works well.

The Outperformance of ‘Winners’ vs. ‘Losers’ in the Market



Source: BlackRock

Cliff appeared at George Mason in 2015 to explain, among other things, momentum as a factor. The ‘rather insane’ proposition is that you buy a basket of stocks that have been going up for the past 12 to 18 months and they will continue to do so. He also appeared at the University of Missouri to present “A Brief and Biased Survey of Quantitative Investing”.

Stillwater View: Most of Wall Street is out searching for answers to the markets unrelenting strength that is lacking both fear and volatility. One of the likely causes is the insatiable appetite for emotionless ETFs that are devoid of the qualitative human factor.

Momentum is probably one of the most interesting quant factors because few on the fundamental side can come close to replicating it. If assets keep flowing into funds of this variety, buying pressure on ‘what’s working’ will continue. Until of course it doesn’t.

While E. Coyote



Source: *Geek.com*

Diversions

Russian fertilizer magnate Dmitry Rybolovlev set a new high watermark for art when he agreed to pay \$450.3 million for da Vinci's *Salvator Mundi*. The estimated value for the piece pre-auction was \$100 million. Four people bid by phone, one was in the room and the gavel fell after 18 minutes. *The New York Times* chronicled the bidding. Andrea Fesltd, a Bloomberg Gadfly columnist, writes "There's Always a Billionaire Medici to Buy Your da Vinci".

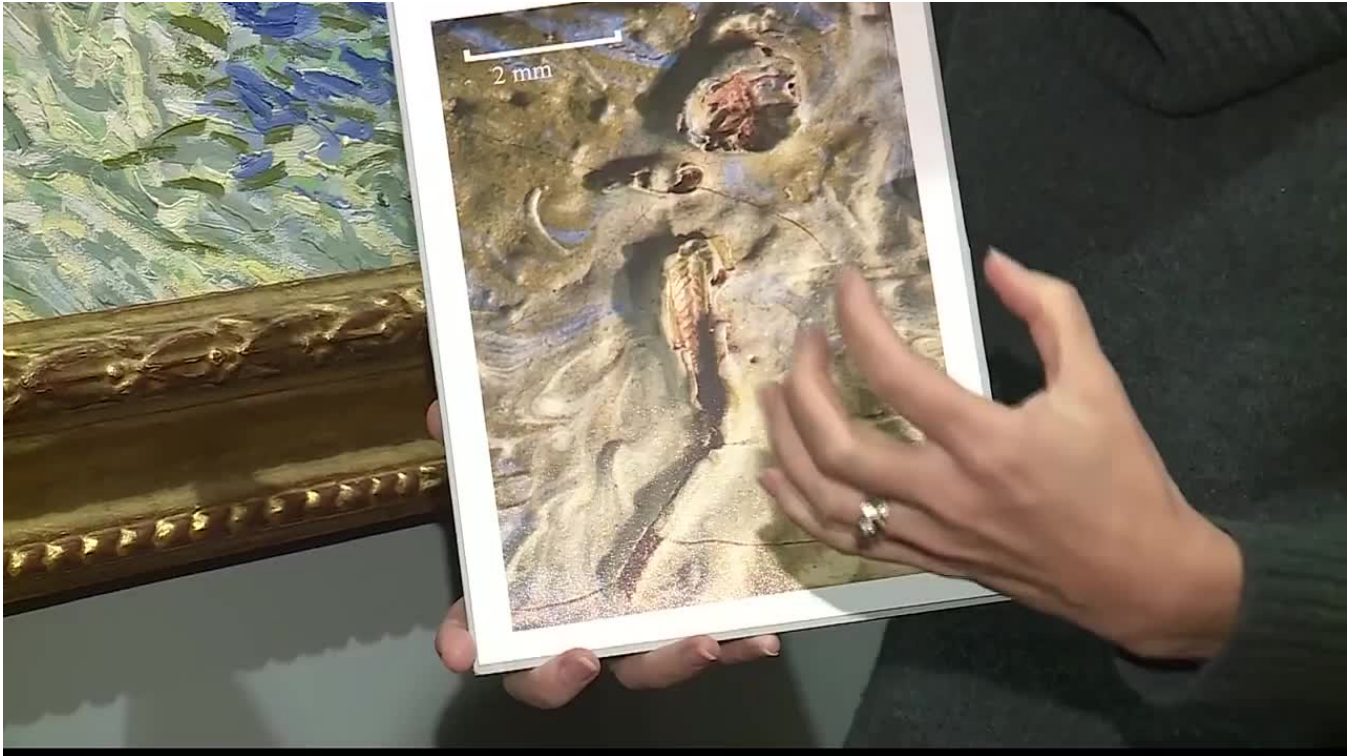
Leonardo da Vinci's *Salvator Mundi*



Source: Artnet News

In other news from the art world, a tiny grasshopper was found in Van Gogh's 'Olive Trees' by a researcher at the Nelson Atkins Museum of Art. It required a surgical microscope to find the creature. Live Science.com provides 11 hidden secrets in famous works of art.

Close-Up of the Grasshopper in Van Gogh's 1889 "Olive Trees"



Italy failed to make the World Cup for the first time in 60 years this week. The web erupted with various forms of comic relief. Misery loves company so much so that there is a movement afoot to create an 'NIT' versions of the World Cup this year that would include the American side.

Italy is Sitting Out the 2019 World Cup



Next week will be a short one on Wall Street as everyone will be shutting down early next Wednesday in anticipation of the Thanksgiving holiday. *The Wall Street Journal* gives us the original '32 Rules of Thanksgiving Touch Football' and "27 More Rules of Thanksgiving Touch Football".

Stillwater Favorite Selection: It's okay to play with kids but don't baby them. Just because your 7-year-old niece is playing quarterback doesn't mean you can't intercept her screen pass and run it back for a touchdown. She's got to learn sometime not to throw into triple coverage.

Grandma Does a Touchdown Dance



Source: The Wall Street Journal

Those searching for a theme for this holiday's culinary festivities need to look no further, as some of the best chefs out there provide their favorite Thanksgiving Day menus. Bobby Flay has his, and so does the famed Alice Waters. Sunset Magazine provides 15 complete recipes. And Justin Devillier, of La Petite Grocery in New Orleans, has a Wonderful Day-After Gumbo.

The Macy's Thanksgiving Day Parade



Source: Family Vacation Critic

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