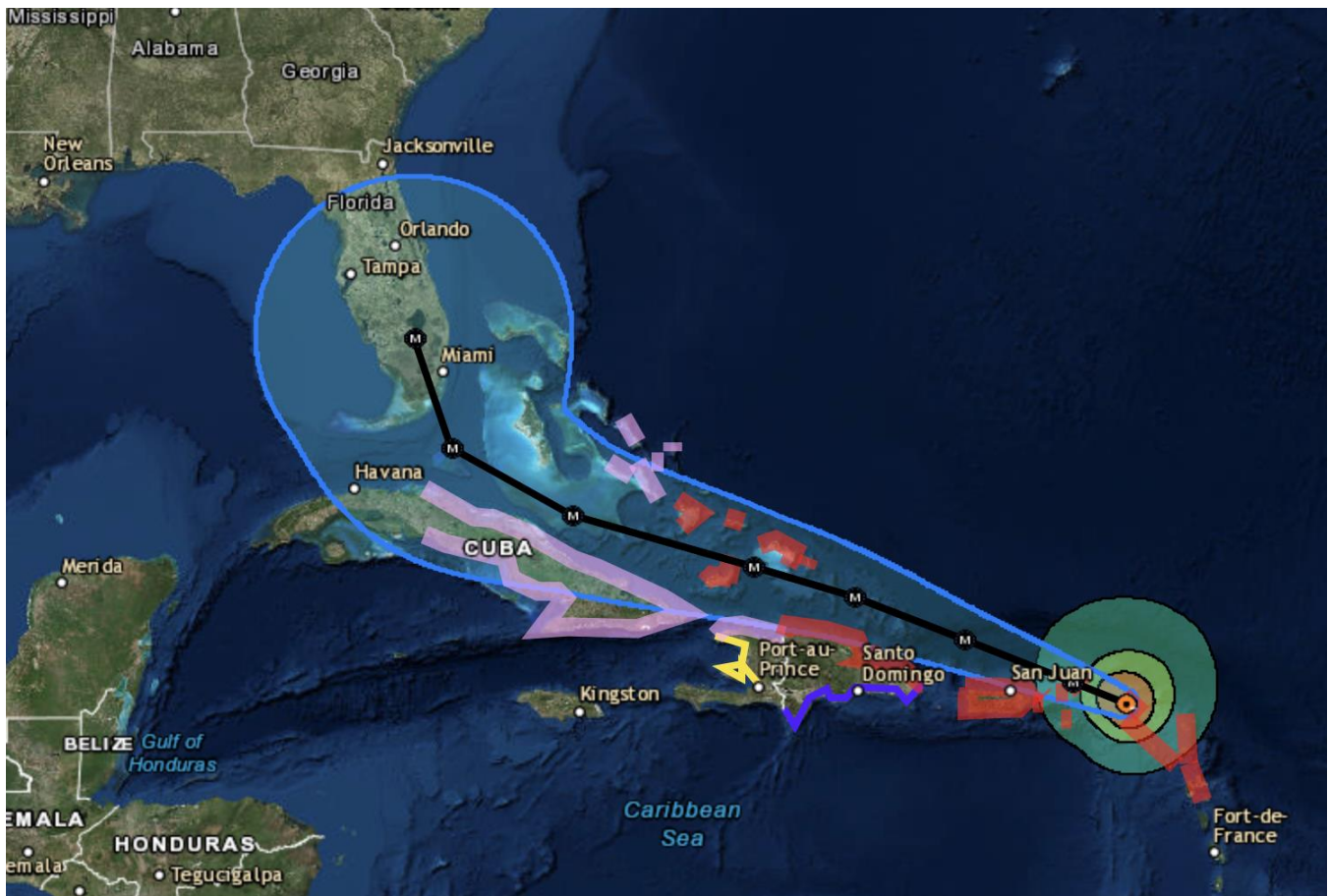




September 8<sup>th</sup>, 2017

The Top-Down

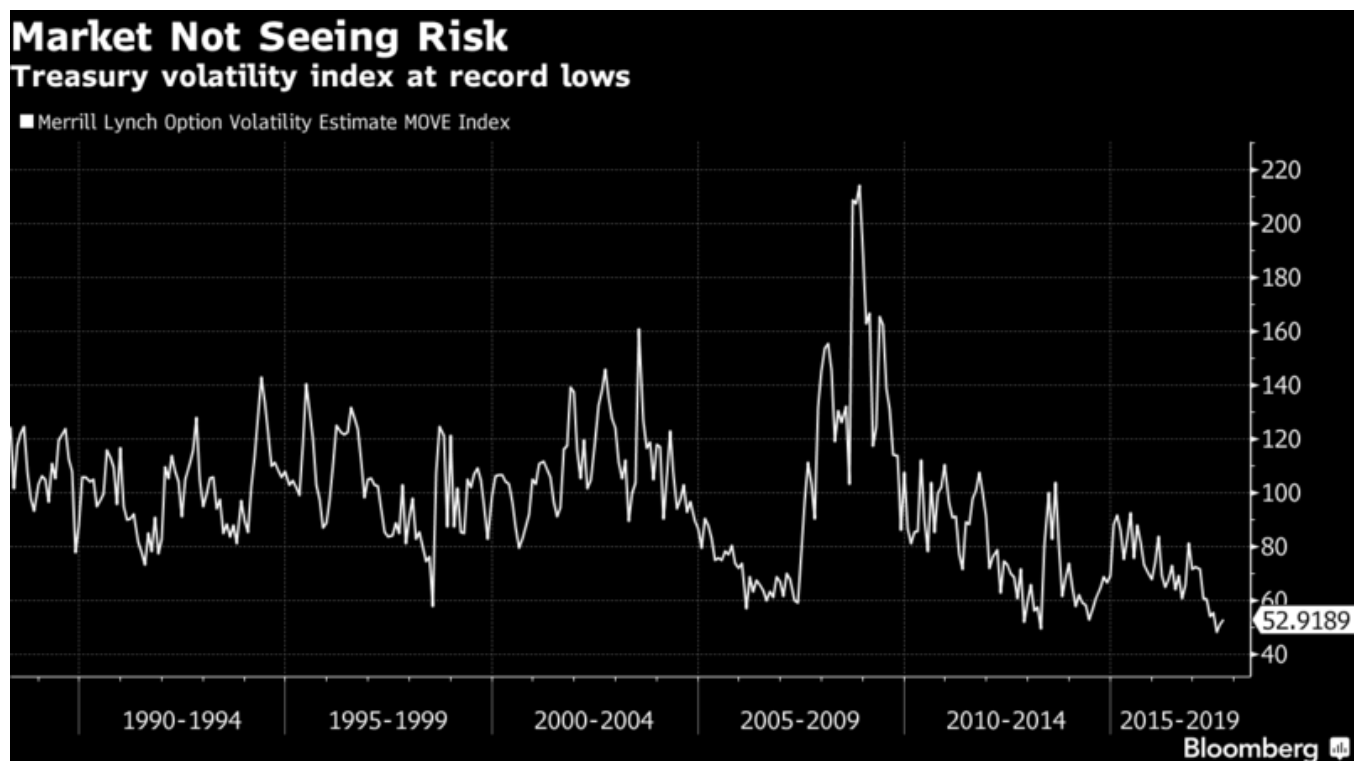
Hurricane Irma is moving through the Caribbean and is expected to make landfall in Florida late Sunday. This category 5 storm is the largest ever recorded in the Atlantic. Property casualty insurers with exposure have sold off in anticipation of significant damage. The astonishing view of Irma courtesy of NASA.



Fed Vice Chairman Stanley Fischer announced that he would be [stepping down](#) in October for personal reasons. His term was set to expire in June of next year. Gary Cohn's criticism of President Trump's Charlottesville remarks may have [cost him the top spot](#) in the organization. Leading to speculation that he [may be on the way out](#) at the White House.

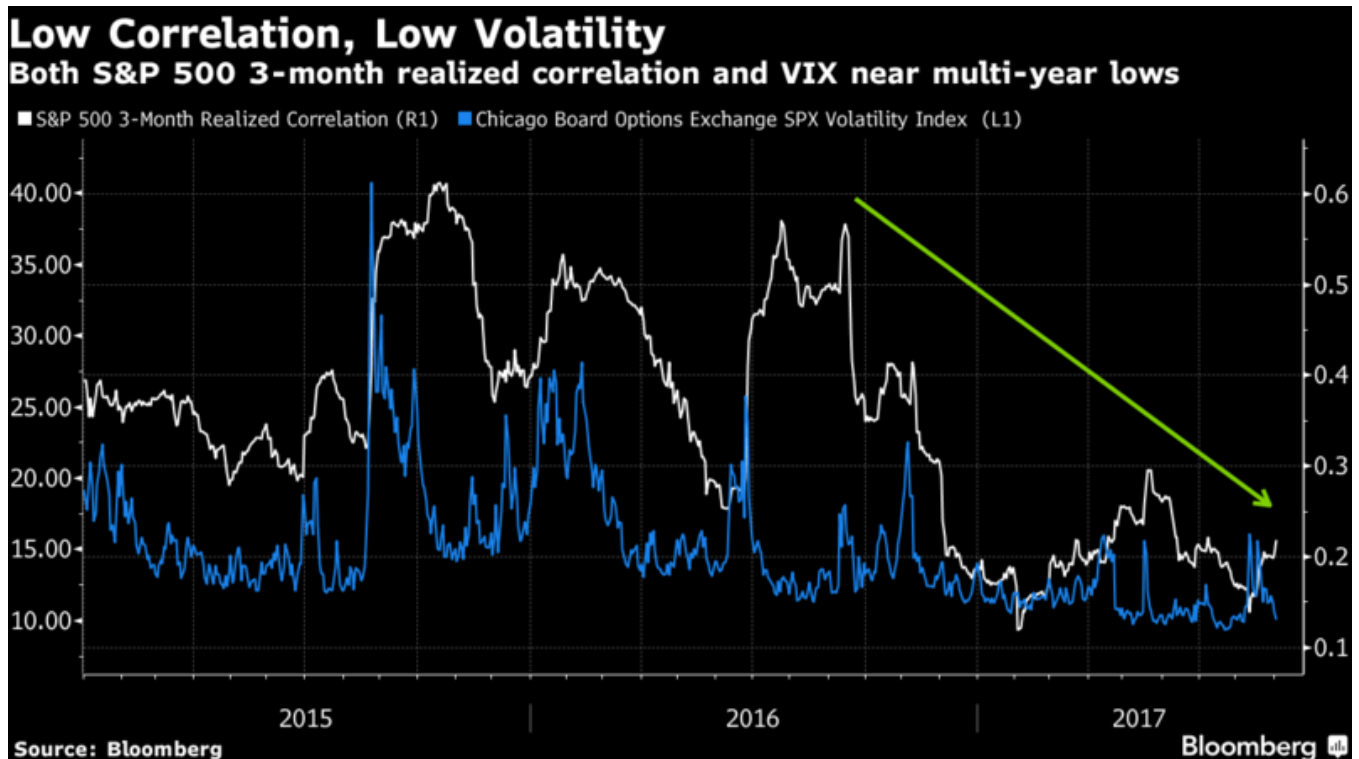
Deutsche Bank's CEO John Cryan is calling for the ECB to accelerate the end of loose monetary policies as asset bubbles are forming and the risk of "[greater upheaval](#)" is growing as they expand. Mario Draghi appears to have [gotten the message](#).

Goldman Sachs CEO Lloyd Blankfein finds it "[unnerving](#)" that yields are [higher on corporate debt](#) than on corporate dividends. Morten Steinland, who manages \$6.6 billion in fixed income at Alfred Berg in Norway expressed similar thoughts. Calling this chart of Treasury volatility "[the scariest graph I see](#)".



*Stillwater View: Risk has indeed been taken out of the markets and they are ill prepared if something goes bump in the night.*

The sector churn beneath the index calm has resulted in a [breakdown in correlations](#). Stock picking, both long and short, has an opportunity to show that it has a place in the market.



While history has shown that it's almost always good to be long the market, it's important to keep returns in perspective. Markets do indeed go through decades of volatile swings. Sometimes showing only modest progress and riding a wild road to get there. Look no further than the twenty-year history of the S&P 500 from the fall of 1997 to the present.

From October 1997 through August 2000 the technology driven bull market returned 65% to investors. The recession and bear market that followed, including the terrorist attacks of September 2001, would cause the broad market to lose 46% in two years' time.

The Fed reacted to the recession with interest rate cuts and a five-year bull market ensued. By the fall of 2007, Treasury Secretary Hank Paulson was so impressed with growth he proclaimed it to be the strongest global economy he had ever seen.

Two years later, at the depths of the global financial crisis, the market had lost 57%. Lehman Brothers would not survive and millions of homeowners would be washed out in a tidal wave of foreclosures. With the situation looking dire, central bankers were forced to dig deep into their reflation handbook. They rolled out round after round of quantitative easing. The result? From the March 2009 bottom to today the S&P 500 has returned an impressive 270%.

*Stillwater View: Why the walk down memory lane? It serves as a reminder that the 6.78% annualized return over the past twenty years has come with considerable volatility. Something that the markets have been eerily devoid of lately. That return includes the roughly 2% contribution from dividends.*

*A modest 10% correction in the S&P would bring the index back down to the 2,200 level with a more substantial fall of 20% resetting it to 2,000. The former is more probable, but the latter is well within the realm of possibility. The market has had an extended rally, valuations are full, central bank policy is shifting and positive economic tailwinds appear to be nearing the end of the runway.*

**The S&P 500 - September 1997 through September 2017. Recessionary periods in grey.**



*The Bottom-Up*

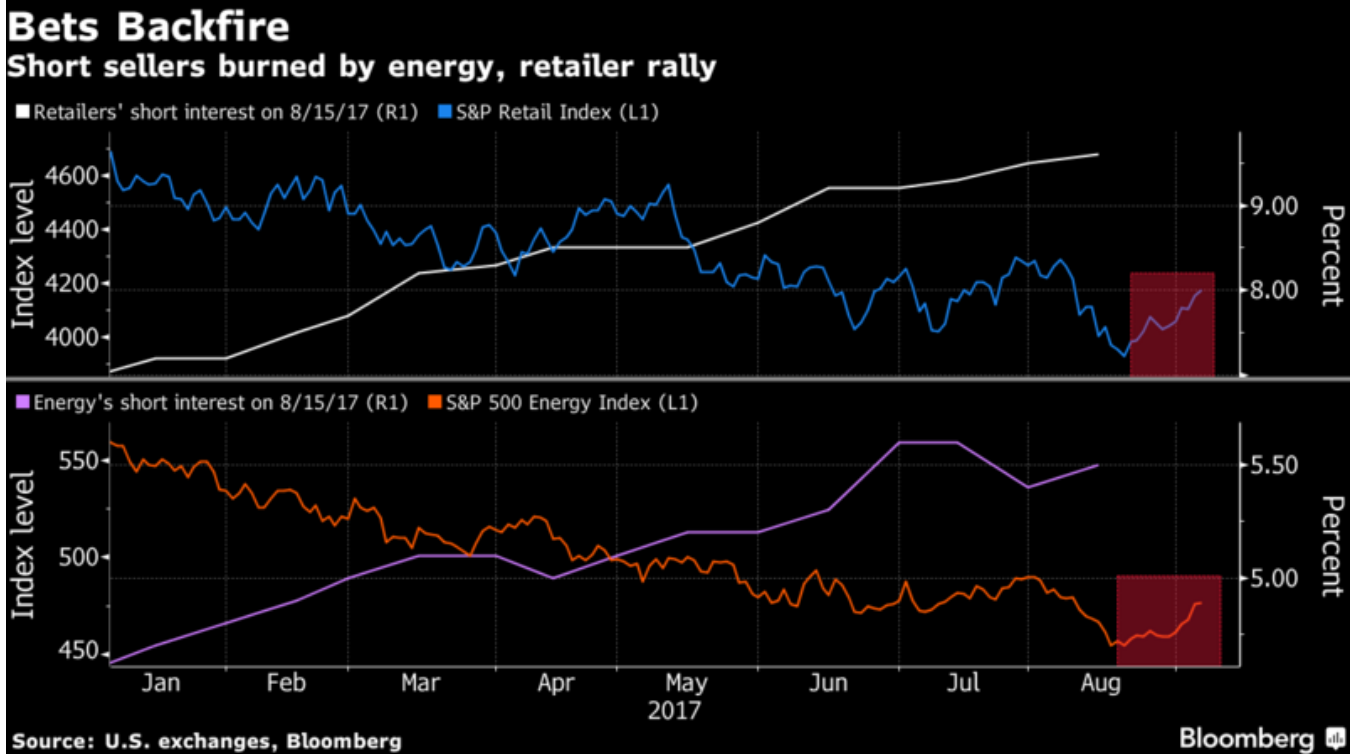
Rovio, the company behind [Angry Birds](#), is preparing to go public and hopes to stay off the list of game developers that have proven disappointments in the market. [Lego is struggling](#) as the company reported the first sales decline in thirteen years. Blaming the slowdown on the continued shift towards [electronic gaming](#) among kids. Meanwhile [Juicero](#) is no more as the \$400 million venture that sat at the crossroads of technology and healthy living closed shop.



Disney CEO Bob Iger commented on Thursday that [current year earnings](#) would be in-line with last year. Wall Street expected modest year-over-year growth and the stock dropped 5% on the news. The company is under continued pressure from Netflix and other streaming options. It has decided to [go it alone](#) in its efforts to compete. Wells Fargo's Marci Ryvicker [upgraded the shares](#) to a market outperform on Tuesday. Hollywood is also coming off the [worst summer](#) since 2006.



The [retail and energy sectors rallied](#) this week as investors searched for value in an otherwise expensive market. This reversal of the hedge fund momentum trade has hurt those who had piled in on the short side of the ledger.



Kohl's decided that if you can't beat Amazon, you [might as well join it](#). They announced the buildout of [dedicated space](#) to market Amazon home products and devices in ten stores located in the Chicago and Los Angeles areas. Restoration Hardware [shares rocketed 40%](#) higher on Thursday when the company raised guidance on increased adoption of the company's membership model. The shares have been heavily shorted this year.



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Apple is gearing up for the [iPhone 8](#) launch next week. Rumors of potential production delays have Bernstein's [Tony Sacconaghi](#) concerned about the impact it could have on the stock.



Meanwhile, the New York Yankees have accused the rival Boston Red Sox of [stealing signals](#) using an Apple iWatch. Turns out the act itself isn't illegal, it's simply limited to the human eye.

### Up and Down Wall Street

Steve Cohen is ramping up to [raise \\$10 billion](#) next year, when his 2016 [settlement](#) with the SEC allows him to start managing outside money again. Cohen appeared with AQR founder Cliff Asness at the Milken conference last year as they discussed [the evolution of hedge funds](#) and the future of asset management. Fortune profiled his comeback in an [extensive interview](#) last fall.



The highly-anticipated book by Ray Dalio, “[Principles: Life & Work](#)”, will be published later this month. Andrew Ross Sorkin writes the [preview](#) for the *New York Times*. Mr. Dalio is the founder and CEO of Bridgewater, the world’s largest hedge fund. His “[How the Economy Works in 30 Minutes](#)” has been watched more than four million times.

He provided his view of the power of [radical transparency](#) earlier this year in a Ted talk geared towards the book’s release. Ray’s first stock purchase was Northeast Airlines with money he earned as a caddy earning \$5.00 a bag.

*Stillwater View: The look inside the post-election strategy session at Bridgewater is a fascinating view for anyone who has ever wondered what the beautiful machine looks like. The video of Ray Dalio on Wall Street Week circa 1982 is priceless, as is the retrospective acknowledgement of arrogance.*



Tail-risk funds, those designed to profit from Black Swan events continue to disappoint as market dislocations have failed to materialize. The [Wall Street Journal](#) reports that the strategies are down 6.5% this year. Man Group's AHL Tail Protect fund has lost 45% since inception in 2009.

### Black Swan Down

Cumulative return of tail-risk funds since December 2007



Source: CBOE Eurekahedge Tail Risk Hedge Fund Index

THE WALL STREET JOURNAL

### Diversions

In case you missed the cozy campout for 70,000 in the Black Rock Desert this year, here is the recap of nine days of [Burning Man](#) in under two minutes.



The [U.S. Open](#) continues today at Arthur Ashe Stadium in Queens with the [men's semifinal](#) taking place this afternoon. The [woman's final](#) goes down on Saturday, matching Madison Keys and Sloan Stephens. The tournament wraps up Sunday with the men's final.



[The Monterey Jazz Festival](#) turns 60 this year and kicks off next Friday. The event, not to be confused with the [Monterey Pop Festival](#) which turned 50 in June, runs through Sunday, September 16<sup>th</sup>. If you find yourself there take the short drive north to Moss Landing and enjoy a bowl of Cioppino like no other at [Phil's Fish Market](#).

Saturday's college football schedule has [games of consequence](#) as "[The](#)" [Ohio State Buckeyes take on Oklahoma](#) at the Horseshoe in Columbus and [USC will host Stanford](#) at the Coliseum. Hard to believe that it was eight years ago that a young Richard Sherman taunted the Trojan faithful and Pete Carroll famously [wondered aloud](#) what Jim Harbaugh's "deal" was. Pete would get his revenge four years later as the Seahawks defeated the Harbaugh coached San Francisco 49ers in the 2013 NFC Championship Game.



*Stillwater View: Have fun out there and don't leave the game early. You never know what might happen with your team down [44-10](#) late in the third quarter. Just ask my wife and kids.*

The NFL season kicked off last night as the Super Bowl champion Patriots were defeated 42-27 by the Chiefs in Foxboro. Big games on Sunday include the [Steelers vs. the Cleveland Browns](#), the [Seattle Seahawks take on the Pack](#) and the [Cowboys face the New York football Giants](#) in an early NFC East showdown. Commissioner Rodger Goodell is first and goal on a five-year [contract extension](#).

*Stillwater View: America's Quarterback Tom Brady and the Patriots will continue their reign as everyone else is playing for second in the AFC. It will be a toss-up between the Green Bay Packers, Carolina Panthers and the resurgent Cowboys in the NFC. The Atlanta Falcons will try to [shake the horror](#) of blowing a 25 point lead in the last Super Bowl. And the San Francisco [Forty Niners](#) will once again give this author his Sundays back as they won't be seeing the playoffs anytime soon.*

[Super Bowl 52](#) takes place on February 3<sup>rd</sup> in the new Nordic modern U.S Bank Stadium in Minneapolis. Las Vegas is giving the [New York Jets](#) a historic 1,000 to 1 shot of getting there.



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