



*July 28, 2017*

*Stillwater Capital*

[Strategic Investor Radio](#) host Charlie Wright and I sat down for an interview last week and the conversation ranged from hedged investing, short selling and the current state of the markets. Charley asks guests to bring with them a book recommendation on investing. My long-standing selection is [Soros on Soros, Ahead of the Curve](#).

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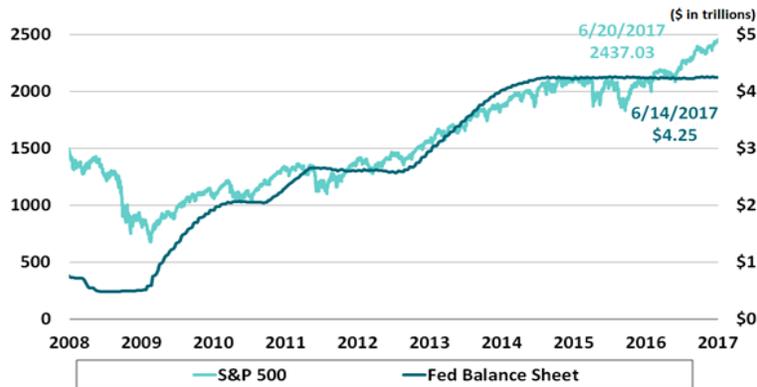
*The Top-Down*

Second quarter GDP [grew at a 2.6% rate](#), in-line with consensus and a solid first look at a number that will go through several revisions. Final Q1 2017 GDP came in at 1.2%.

The Federal Reserve held off on [raising interest rates](#) this week as balance sheet normalization [takes pole position](#). The unwind, and what it means, [according to CNBC](#). Steve Liesman reported the results from the most recent investor survey finding a wide belief that the Fed was on hold and a growing consensus that a "[significant correction](#)" in the market was on the horizon.

On Thursday Blackstone's Byron Wien shared his view that there are [Some Speed Bumps Slowing the Bull](#). "Since the beginning of 2017, the balance sheet has remained flat and the index has risen almost 10%. This divergence is disturbing, particularly since the Fed is contemplating a balance sheet shrinkage starting in September. The combination of small increases in productivity and tighter monetary policy represent an obstacle to the market for the second half of 2017. Earnings are coming though impressively, however, and I still believe that we will see higher highs for the index before Christmas."

Fed Balance Sheet Versus S&P 500



Source: Gavekal Research, Evercore ISI (6/17).

*Stillwater View: The correlation between the Fed balance sheet and the S&P500 is no secret on Wall Street. Rhetorically speaking, is it possible that everyone is now discounting the same thing?*

Oaktree Capital chairman and co-founder [Howard Marks](#) joins those [advocating caution](#) given his view of the current environment. In his most recent memo, [There They Go Again...Again](#), Mr. Marks observes that,

- **The uncertainties are unusual in terms of number, scale and insolubility** in areas including secular economic growth; the impact of central banks; interest rates and inflation; political dysfunction; geopolitical trouble spots; and the long-term impact of technology.
- In the clear majority of asset classes, **prospective returns are just about the lowest they've ever been.**
- **Asset prices are high across the board.** Almost nothing can be bought below its intrinsic value, and there are few bargains. In general the best we can do is look for things that are less over-priced than others
- **Pro-risk behavior is commonplace**, as the majority of investors embrace increased risk as the route to the returns they want or need.

*Stillwater View: The size of the chorus advocating caution is beginning to rival that of the Mormon Tabernacle. But it's not just the number, it's the quality. Jeff Gundlach, Ray Dalio, Bill Gross, Howard Marks, Byron Wien, the PIMCO Investment Committee are all seemingly on the same page. While it's possible they collectively get it wrong, it's not likely.*

*The Bottom-Up*

This was a big week for earnings as 550 companies reported on Thursday alone. The reactions to each showed the depth of fundamental crosscurrents beneath the otherwise placid indexes.

Boeing hit new record highs on the back of a [“nearly perfect”](#) earnings report. Cost cuts helped, but so did the [787 and 737](#) finding their production sweet spot. Caterpillar provided a similar report with cost controls and [strong global demand](#) for equipment driving quarterly profits higher. Fast casual dining suffered as the struggles at [Outback Steakhouse](#) and [Buffalo Wild Wings](#) continue.

FaceBook reported on Wednesday and the Street [loved what it heard](#). Advertising sales slowed, but cost per ad accelerated. Bloomberg’s Shria Ovide says [Don’t Worry be Happy](#).

At \$170 a share, the company’s market capitalization stands at nearly \$500 billion. Not bad after suffering a rocky start out of the gate as FB traded below \$18 in 2012. A perfect purchase then, held through this week, would have netted an 800% gain. The guy in the grey hoodie and the big smile seems to have figured something out.

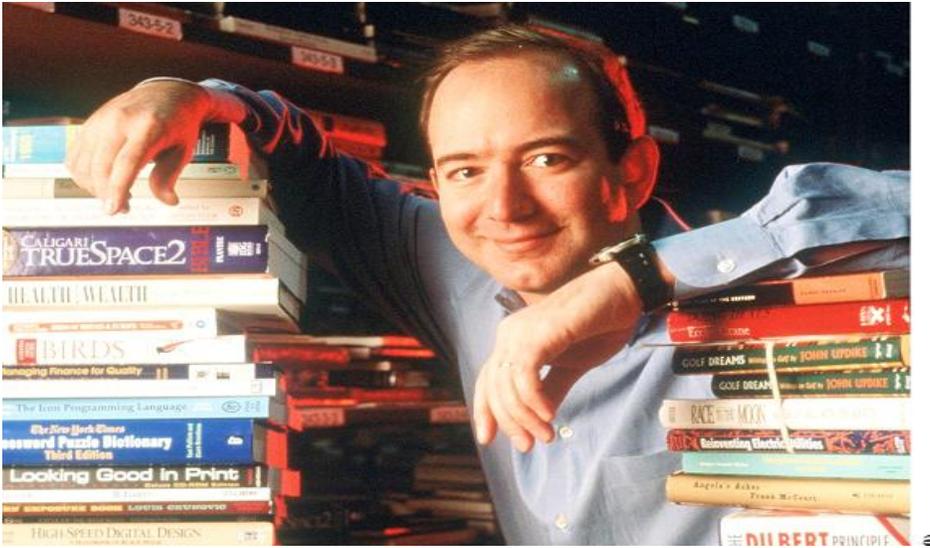


*Stillwater View: This week was filled with high expectation, high valuation and underperforming sectors that caught fire on Thursday as technology began to fade. There were huge moves higher in retail and media as well as energy. It’s not the rotation that is surprising, it’s the speed and velocity at which it occurs that makes the head spin.*

### Up and Down Wall Street

Vanity Fair Special Correspondent, William Cohan, [discusses with WNYC](#) the [“Untold Story of How Gary Cohn Fell for Donald Trump”](#).

Bloomberg provides a [visual roadmap](#) as to how Jeff Bezos became the world’s wealthiest person. The guy in the blue button-down and the big smile seems to have figured something out.



[The Bezos Empire](#), in one chart.



Dan Loeb and Third Point have been doing right in 2017 as the [“fading Trump trade”](#) has seen a roundtrip. The fund is up 10.7% though the end of the second quarter. In his most investor letter he discussed why he likes [BlackRock](#) as the world’s largest asset manager becomes increasingly networked. In a world where candor is sometimes hard to come by, you should appreciate the kind Mr. Loeb’s has shown as he admits that none of his macro predictions from earlier this year have come true.

### Diversions

The [Great American Solar Eclipse](#) is fast approaching, as the “path of totality” will touch down exclusively in the United States on August 21<sup>st</sup>. Make America Dark Again! [Jackson Hole](#),

[Wyoming](#) has become the western states epicenter for the event. Good luck [finding anything](#) that resembles a room as 80,000 people are expected to descend on the Snake River Valley.

The *Wall Street Journal's* Off Duty covered [fishing excursions](#) where casting a line isn't the only fun to be had. If your travels take you to Bozeman this summer give the guides at [Montana Troutfitters](#) a call. They will have you living the fly fishing dream of pulling a culvert hanging brown from a spring creek in the middle of a Target parking lot. True Story!

Home values in the [Hamptons](#) have reached [new records](#) as properties like [Tick Hall](#) list for more than \$60 million. Less than half the [\\$140 million asking price](#) for East Hamptons 100 & 90 [Briar Patch](#) road. The most expensive residential listing in the country. This [oceanfront estate](#) on 17 Mile-Drive in Pebble Beach will not only put you in position A for the [2019 U.S. Open](#) but also set you back a cool \$45 million. [Jackie Kennedy's](#) childhood home near McLean, Virginia is also available for those with the \$50 million in [historic means](#).

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