'What's left of summer, but a fading rose'

Just to show our range and versatility, we aren't afraid to lead with a van Gogh and a showtune lyric from La Cage aux Folles. Because it is indeed the waning days of summer 2019, and hopefully for you, yours, and your close friends, these are the best of times, for what's left of summer, but a fading rose.

Stillwater is wrapping up what has been a great first two thirds of the year and are dialing ourselves in for what should be a very eventful upcoming four months, at least that's what we are planning for. As a reminder, adjust for volatility when you can, not when you have to.

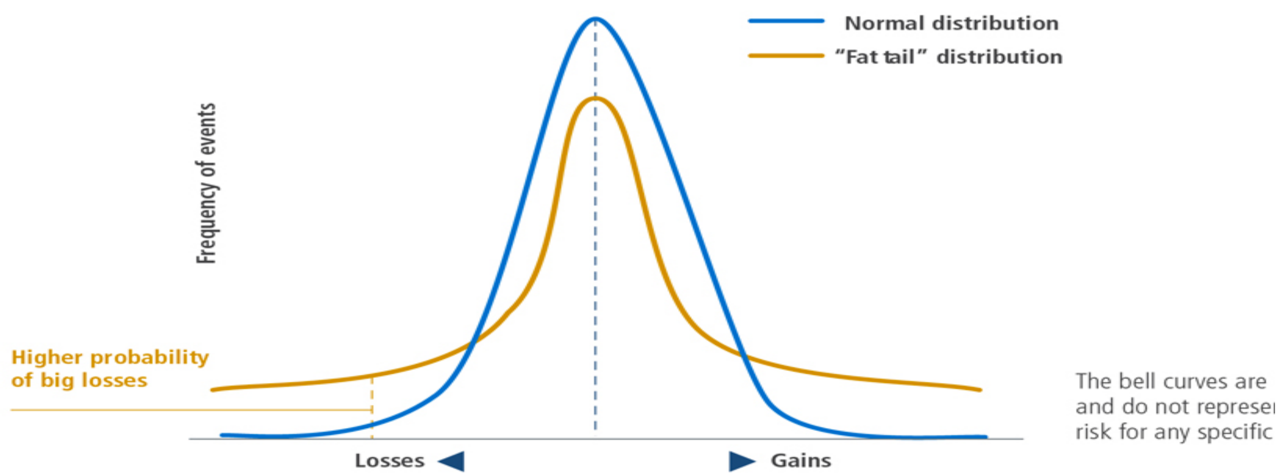
Sea & Sick

Quick programming note, next week these pages will include the addition of four new names to the 'bubble basket', a timely position we have been working on for a while now and plan to put into place this month. We will also look at the pre-market futures market, and how it has come to sometimes dominate the day's trading. Finally, as we believe we are entering a period of increased 'tail risk', we are going to deep dive on the subject, which will also give us a chance to once again de-mystify the alternative investment side of the investment spectrum.

For Whom the Bell Curve Tolls

FIGURE 1: MARKET TAILS MAY BE "FATTER" THAN NORMAL

Tail events are very rare in a normal curve, but market tails are in fact "fatter," or more frequent, than many people realize.



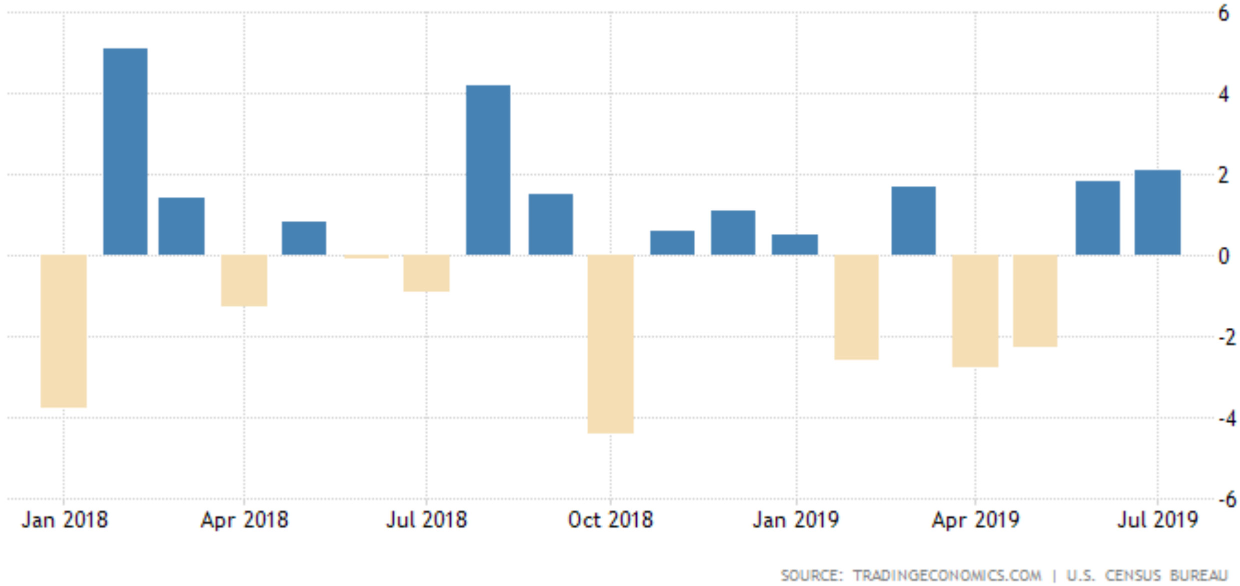
Source: Pimco

The Economy

Aside from a bunch of G7 led theatrics, and phantom phone calls between the U.S. and China trade reps, it was a week to get back to the hard numbers that are shaping the economic debate. Strap in for a quick whip around the many releases that came across the tape.

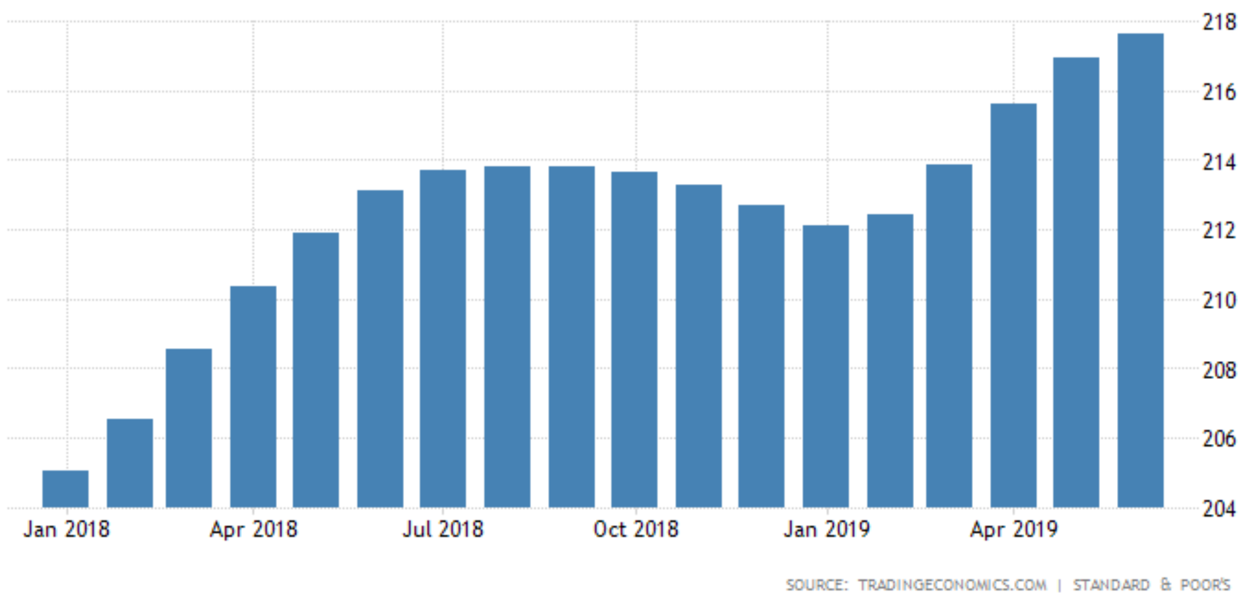
In a sign that perhaps the industrial economy is not falling off a cliff, durable goods orders appear to have stabilized. Evidence of why this number is important could be seen last year when the mid-year spike higher appeared to confirm that the we were on sound footing. Fast forward to December, and the number appeared to confirm our worst fears, and the market reacted accordingly.

Durable Goods Orders



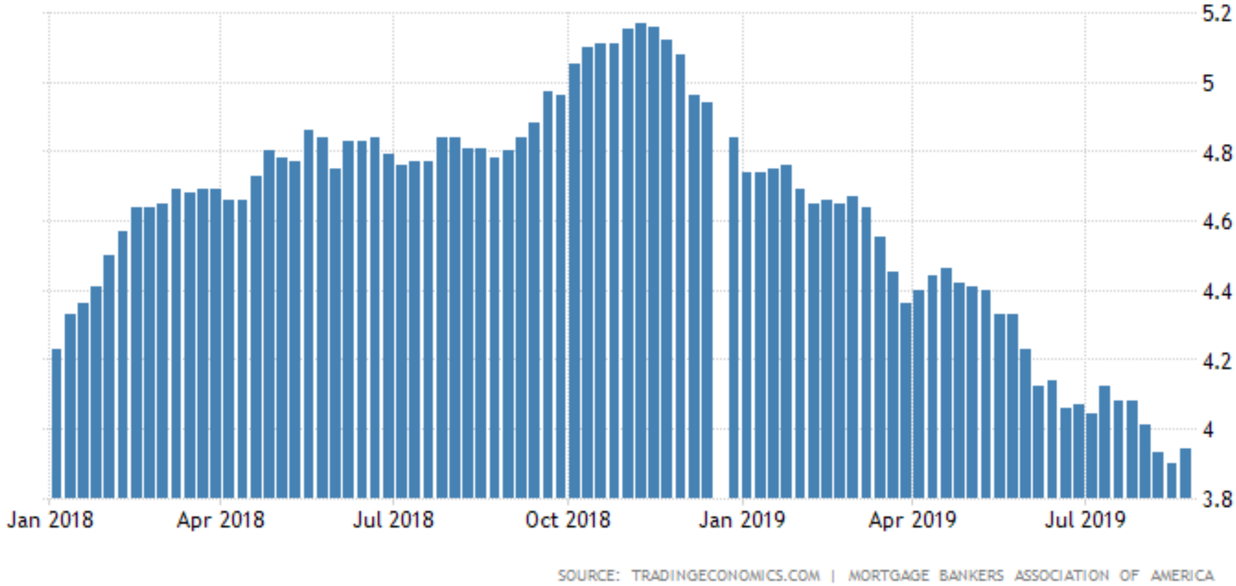
In another sign that Powell's pivot on interest rate has had a positive effect, the Case-Schiller home prices index continues to reach new highs, this after a second-half of 2018 swale.

Case-Schiller Home Price Index



The biggest driver to this is the plunge in mortgage rates and a newfound affordability from cheaper money to finance a purchase. From one year ago, they are now 20% lower. The hottest markets continue to be Phoenix, Tampa, and Las Vegas. Meanwhile the centers of money and power; San Francisco, New York, and even Seattle are showing signs of moderation, and in the case of the latter, even going down.

Rate on a 30-Year Fixed Mortgage



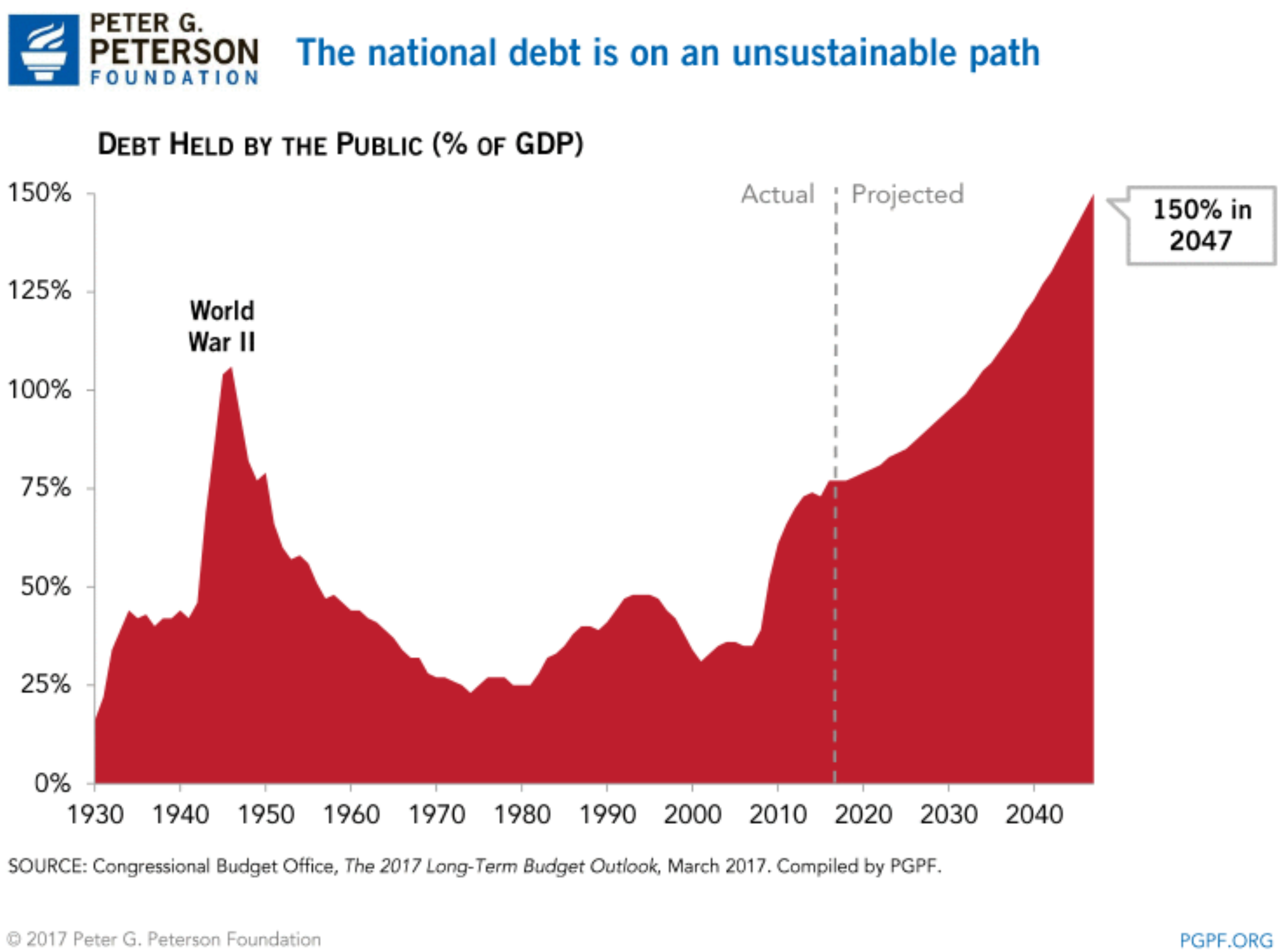
Consumer confidence

The second revision to Q2 GDP came in slightly higher than the Street expected, posting a gain of 2%. Taking a longer five-year look at growth, the U.S. economy continues to fire at an average of roughly 2.5%. Notice again the deceleration seen in the pre-pivot fourth quarter of last year and in the pre-2016 election fourth quarter of that year.

GDP

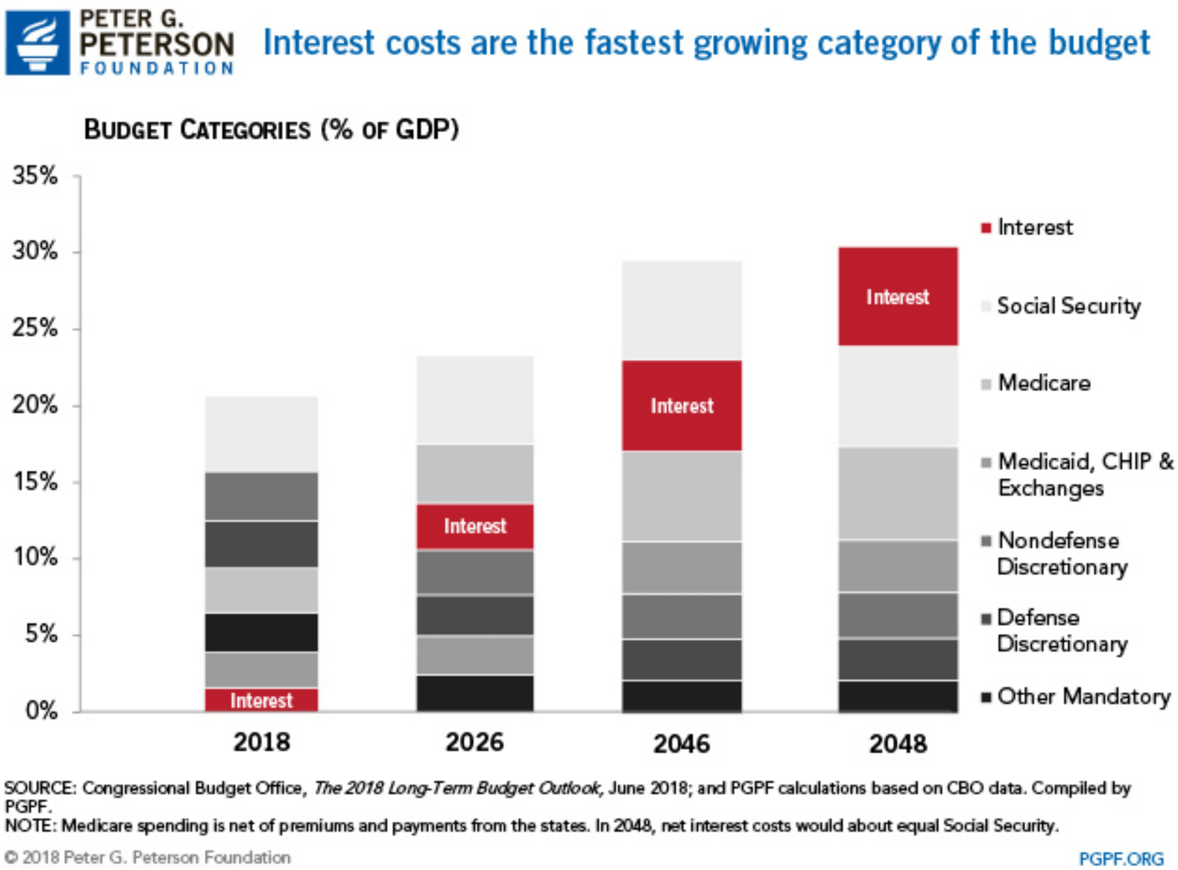
And now for some good news, the public is becoming more aware of the deteriorating situation with the national debt. The bad news, nobody in Washington D.C. cares as the 'deficit hawk' is an extinct bird.

A Hockey Stick Nobody Wants



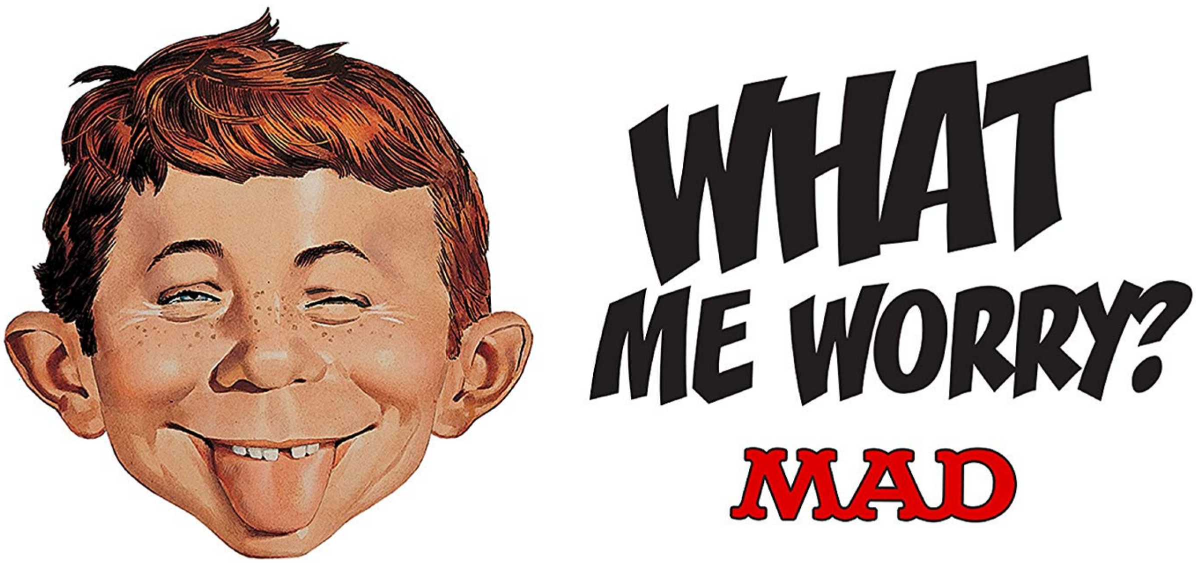
If the projections from the Peterson Institute are correct, in thirty years the interest on national debt will be the single biggest government expenditure, followed by social security, Medicare, and Medicade. This stands in stark contrast to the world we are living in today.

The Tables are Turning



Why do we bring this up? Because more and more smart people are starting to point to the imbalance and potential risk down the road. Included in that are DoubleLine's Jeffrey Gundlach, who calls the deficit 'totally out of control'. Also in this camp are the Wall Street Journal, and economist David Henderson at the Hoover Institute. In a shock to very few, the New York Times and Washington Post are also worried.

One guy who isn't concerned currently calls 1600 Pennsylvania Avenue home. Another one is Larry Summers, who graces our pages twice this week, and thinks we can re-fi our way through trouble partially with lower interest rates. For now, the thoughts of Alfred E. Newman rule the day.



Bill Dudley, The Fed, and President Trump

This week, former New York Fed Chair, Bill Dudley, wrote an unprecedented opinion piece in *Bloomberg* where he said that the Federal Reserve should not enable Donald Trump for what he believes to be ill-advised trade policies, and an overreach in terms of how the president is attempting to influence the independent body's decision making.

"I understand and support Fed officials' desire to remain apolitical. But Trump's ongoing attacks on Powell and on the institution have made that untenable. Central bank officials face a choice: enable the Trump administration to continue down a disastrous path of trade war escalation, or send a clear signal that if the administration does so, the president, not the Fed, will bear the risks — including the risk of losing the next election."

Reaction to his comments were t as unprecedented as the remarks himself. Left leaning *Slate* responded "Please Be Quiet, Sir". *The American Spectator* claimed that he had just Out-Trumped Trump. Bill Clinton's Treasury Secretary, Larry Summers, called the comments 'grossly irresponsible'. Senate Banking Committee member, Tom Tills, is so concerned he has called for hearings to discuss the subject and make sure the Fed doesn't tamper with Decision 2020. What Dudley wrote really cuts to the core of an important issue and is well within the realm of a reasonable argument.

“Officials should state explicitly that the central bank won’t bail out an administration that keeps making bad choices on trade policy, making it abundantly clear that Trump will own the consequences of his actions.”

Former Fed Governor Bill Dudley

Source: Washington Post

Since the trade war has escalated and the Federal Reserve pivoted earlier this year, the markets have taken on a once in a lifetime feeling that there is a perfect hedge in place, and an even more perfect ‘put’ in place. While we agree with those who think economic sabotage from the world’s most important central bank is a bad thing, we don’t disagree that the Fed should sit there ready to put out the fire when the President of the United States is pouring gasoline and lighting matches in the general direction of the global economy.

The Fed as Baking Soda, Salt, and an Extinguisher

Source: Strike First USA

Dividends

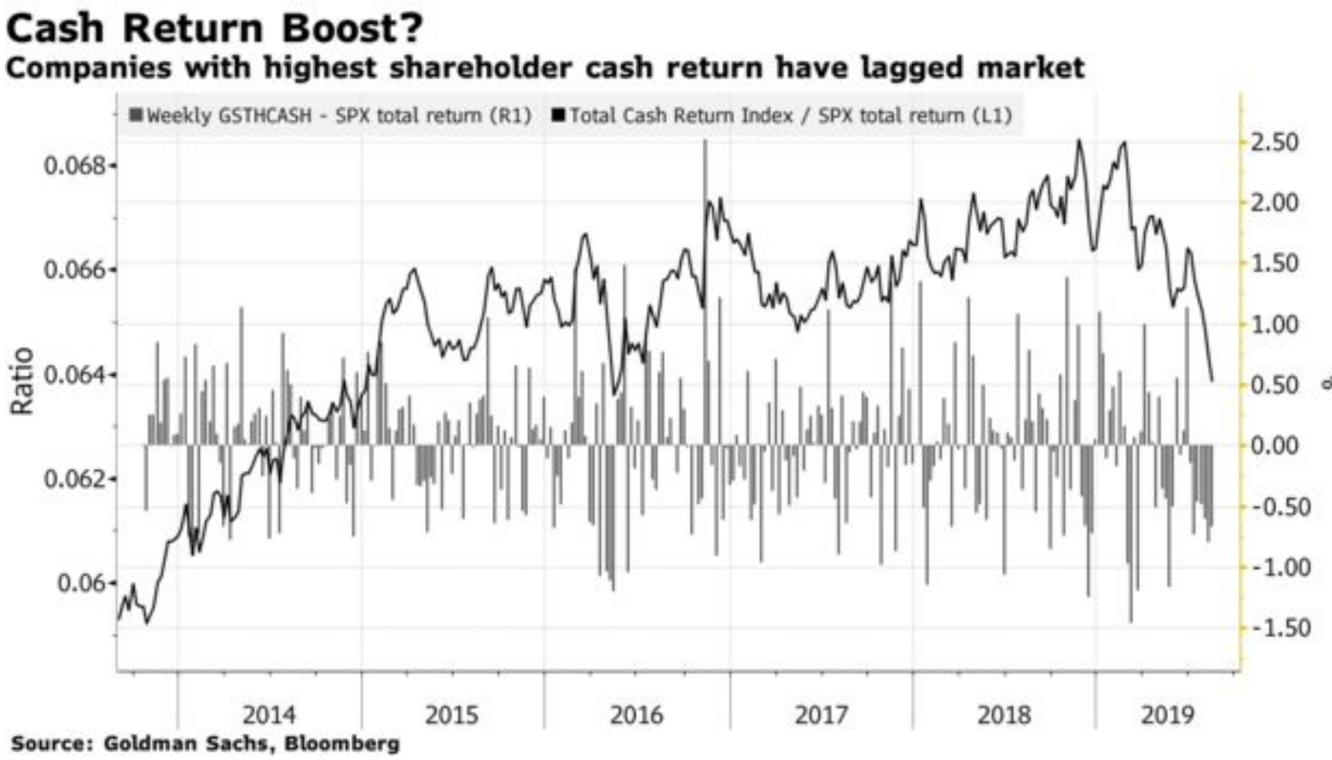
As was reported by *Barron's* last week, dividend growth has slowed materially from last year's strong 14% growth rate. The details of the deceleration were provided by Janus Henderson's quarterly Global Dividend Index. Though the headline of 1% global growth looks frightening, if you strip away currency headwinds you wind up with something more like 4%, which is still worth banking on as four out of five dividend paying companies are increasing their payouts.

Good, Not Great

Source: Janus Henderson

While not as robust as 2018, it's to be expected given the global growth headwinds, that the decision by companies to dedicate more cash flow to share buybacks will continue. Presenting the flipside to the belief that this is best use of cash, *The Atlantic* ran an article in August skewering the practice. *Bloomberg* also threw some shade recently as well.

Where Did the Money Go?



Bringing the subject back home to what we do at Stillwater, our strongest strategy of the past year and a half has been our Hedged Equity Income portfolio. Anchoring the return objective of a smooth 12% to 14% is the 2% dividend yield thrown off by the underlying companies that share the common thread of stable balance sheets. Add to that an 8% to 10% in capital appreciation target, and another 2% to 4% in hedging and short selling proceeds, and you can see how we get to our target. Those interested should inquire within: contact@stillcap.com.

Markets

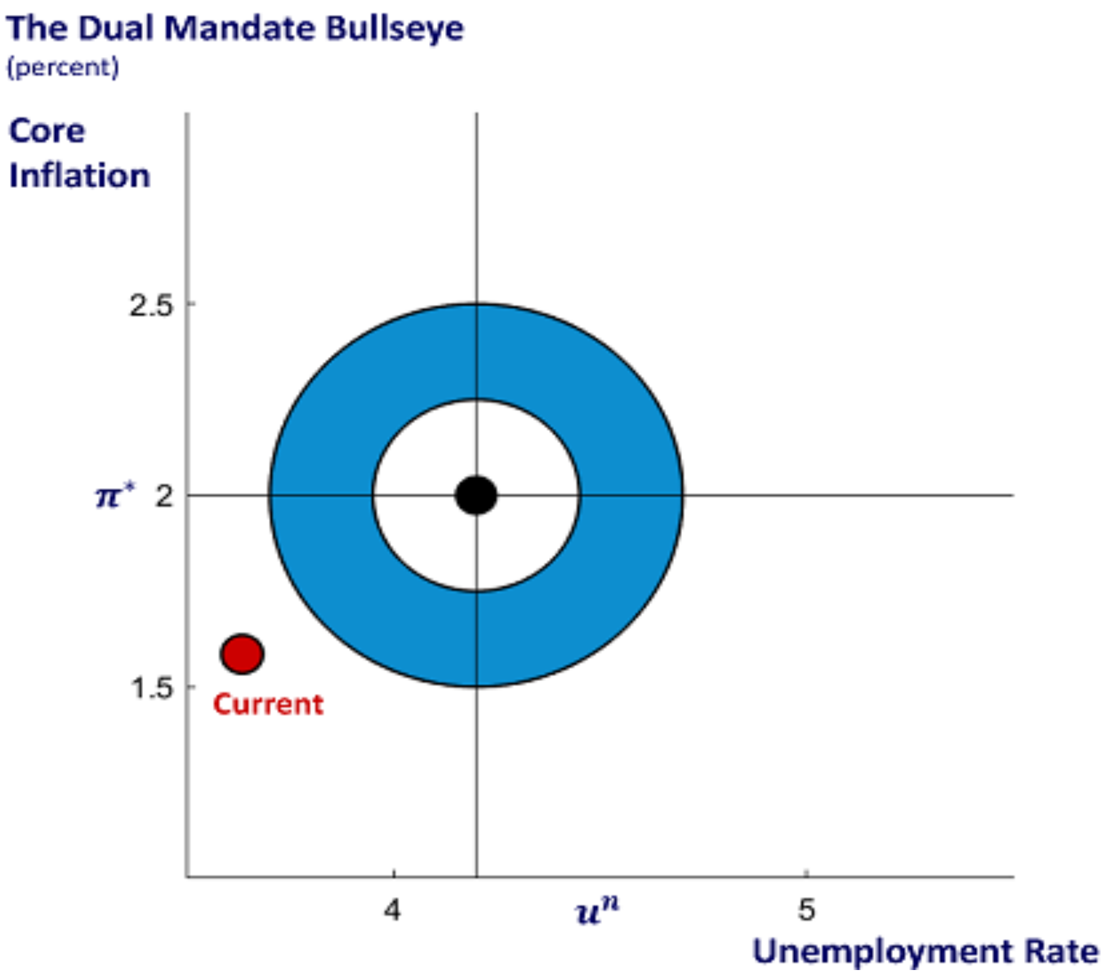
As the *Wall Street Journal* recently pointed out, stock correlations have spiked in August as a binary 'recession or no recession' mentality has taken hold. This type of environment can be exceedingly frustrating for investors and active portfolio managers who must take into consideration a set of circumstances that throw rocks in the gears of trying to project growth out into the future.

In Harmony

Source: Beatles Covers

First Ballot Wall Street Hall of Famer, Byron Wien, provided his thoughts last month on the nuances of the yield curve inversion, and how the Fed has gone beyond the mandate of low inflation and full employment. According to Byron, they have achieved that goal and should do nothing with rates. He added that they are very sensitive to what markets and stocks are telling you, that we are in good shape and that the underlying economy is strong. That said, we find it troubling that the mandate has shifted without a policy statement about that same truth from Jerome Powell.

Good Luck Shooter

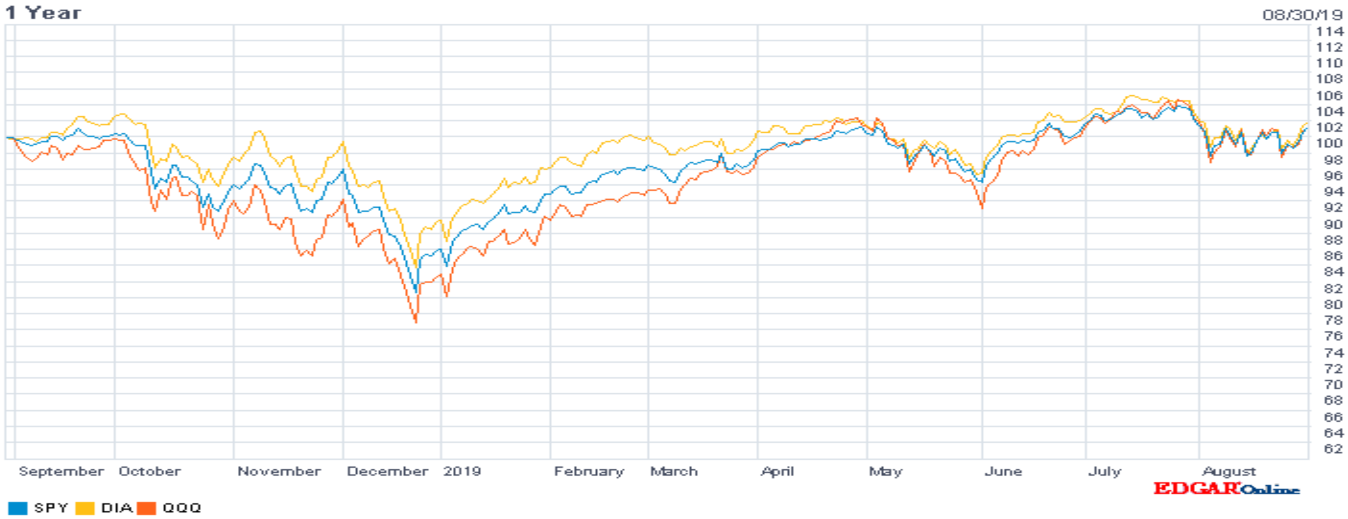


Source: The Chicago Federal Reserve

While Wien doesn't see a recession in 2020, he notes that when one does arrive it will be tougher to combat. This is similar to our opinion that the Federal Reserve hasn't gone far enough this time to re-stock the barrel with dry powder.

In Blackstone's third quarter look ahead, he and the company's Chief Investment Strategist Joe Zidle, painted a solid picture of the economy, while making the Case Against a Melt-Up (or Meltdown). Those of you who consider yourselves thoughtful watchers of the market and economy, should give the webcast the 48 minutes it deserves.

Vol Not Progress – SPY, DIA, QQQ



Up & Down Wall Street

If 'The Big Short's' Michael Burry is at all correct, the bubble in passive investing is upon us, and when it bursts there will be a renaissance for those who fancy themselves good stock pickers. With passive flows remaining strong, this is just hope. But as Andy Dufresne wrote to Red in the 'Shawshank Redemption', 'Hope is a good thing, maybe the best of things. And no good thing dies'. At least that's our hope as well.

Andy & Red

Source: Shawshank Redemption

Diversions – Welcome to Fall

While we recognize that goodbyes are a simply a part of life, we are way more bullish on a hearty hello. With that, we bid summer 2019 adieu and embrace what the rest of the year has to offer. From football, fall art and music festivals, and the coming of the holidays, we have much to look forward to. So, let's bring on the fall.

To Every Season

Source: Yoga Healing Nature

Those looking for answers to the eternal question of why not to wear white after Labor Day, *Town & Country* has you covered. It turns out there isn't one simple answer but a collage of several. The first incarnation was believed to be based on the desire to distinguish those who belonged, from those who didn't. If you didn't show the ability to turn the calendar on your wardrobe, you were the latter.

The second theory was that white was simply interpreted as a summer color that was designed to cool, more appropriate for the beach and golf course than Christmas Parties. Finally, designers and retailers had to move new product. What better way to tie the fall selling season into the fall than selling the story that white was better served May through August, all of which seems reasonable. The turning of the leaves didn't hurt either. That said, Tom Wolfe didn't show the rule very much respect.

The Man in White

Source: Time Magazine

Aside from the Fall Classic in baseball, nothing gets us more fired up about sports than when our football teams lace them up for another season of play. While Tom Brady and the Patriots continue to strangle the life out of the NFL with their dominance, the table is wide open in the college game. Plus, nothing beats the combination of ESPN's College Gameday, the wafting smell of a good tailgate, the hopes and dreams that this is your year, and of course catching the Hawaii vs. whoever game at 9:00 pm Pacific, midnight on the East Coast.

Desmond, Reece, Corso, and Herbie

Source: ESPN

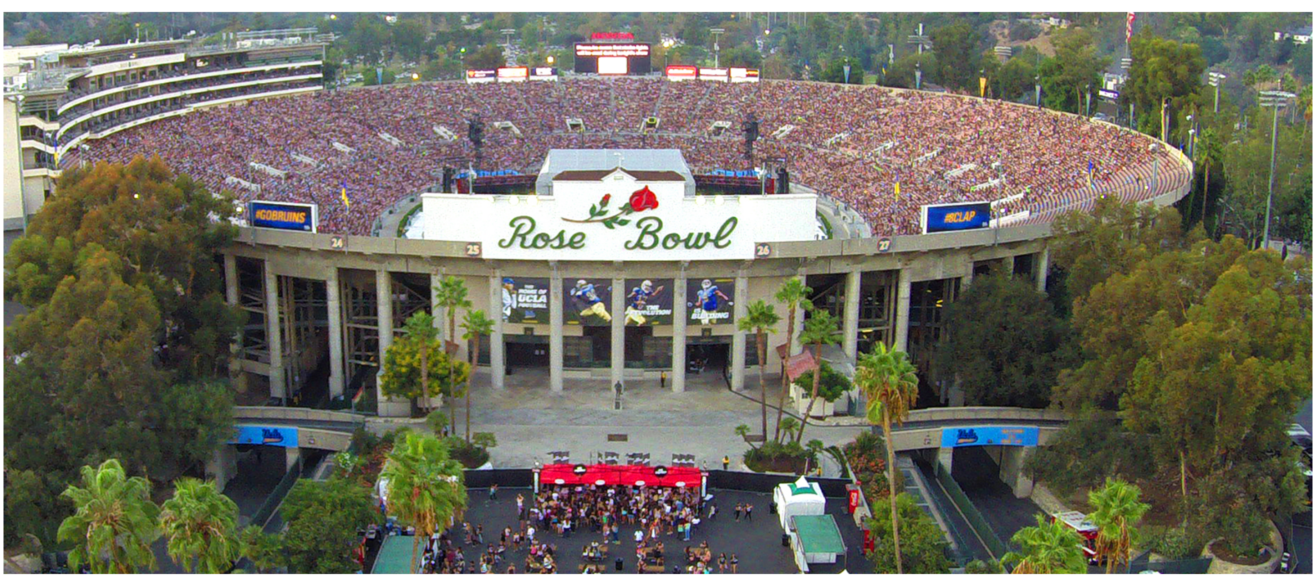
ESPN recently profiled the Best 50 College Football Programs in the country. Sadly, the once proud Bruins from Westwood didn't make the list, but in a shock to nobody, Alabama did.

Roll Tide…again!

Source: Tide 1029

Fox Sports ranked UCLA the number one underperforming program in the country of all time. And that was in 2015. Since then we have produced ten wins and twenty-five losses, including one to the mighty Bearcats of Cincinnati last Thursday night. The good news, the boys in powder blue play in what ESPN calls the greatest venue in the college game.

The Rose Bowl



Source: TCL

As promised, we will be back next week with a full rundown of both the college and pro game. In the meantime, enjoy what can only be described as one of the greatest songs ever to get you in the mood for football. Thank you Kenny Chesney and your ode to the Boys of Fall.

A Beautiful Thing

Source: Un-Afraid Sports