Is It Really Sunny and 72?

As we read through our lineup for this week's edition of This Week in the Markets, we realized that a reasonable person might conclude we have a confirmation bias more attracted to news that isn't predicting the forecast to be Sunny and 72. The reality is, there is still a lot going right with our economy today. Which doesn't mean it couldn't turn south rather quickly, but there should be an acknowledgement with headline risk aside, things aren't that bad at all. Banks earnings this week are proof of that. With this out of the way, now it's on to the rest of the news.

The Economy

Bloomberg's recession indicator is running at the highest level it has seen in a year, and currently sits prognosticating a 27% chance there will be an economic tumble in the next 12 months. The article is a data junkies dream come true, as there are several charts to describe not only how the number is derived, but how also the readings correlate with past contractions. Good news for the bears, risks are rising. On the flipside, the bulls get to point out that the current reading is far lower than it was prior to the last recession in 2008.

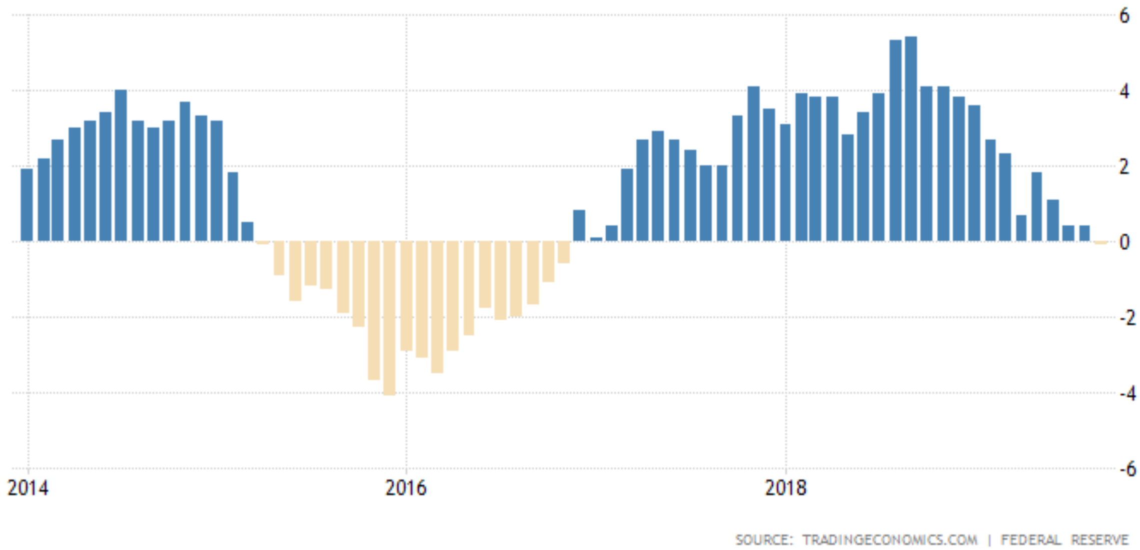
Risky Game

Source: Worthpoint

In September, industrial production slipped into negative territory for the first time in three years, decreasing a whopping .1%. Regardless of the magnitude, the trend is not our friend right now. That said, the reading was negative for almost a year in 2015-2016 and the economy didn't enter a recession.

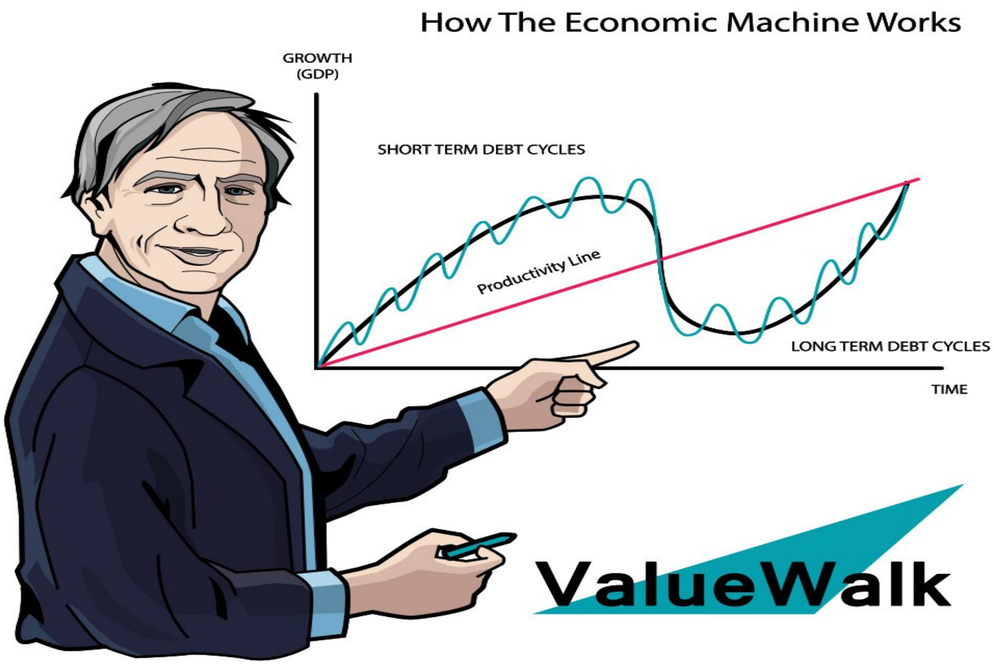
In fact, one could argue that if the U.S. and China can reach a trade deal, and interest rates stay abnormally low, we could be in for a late cycle rebound that would take growth further out into the cycle, and with it a second term for Donald Trump. No taking political sides as we don't do that here, we're simply measuring scenarios based on data and historicals that have decent chances of coming true.

Industrial Production



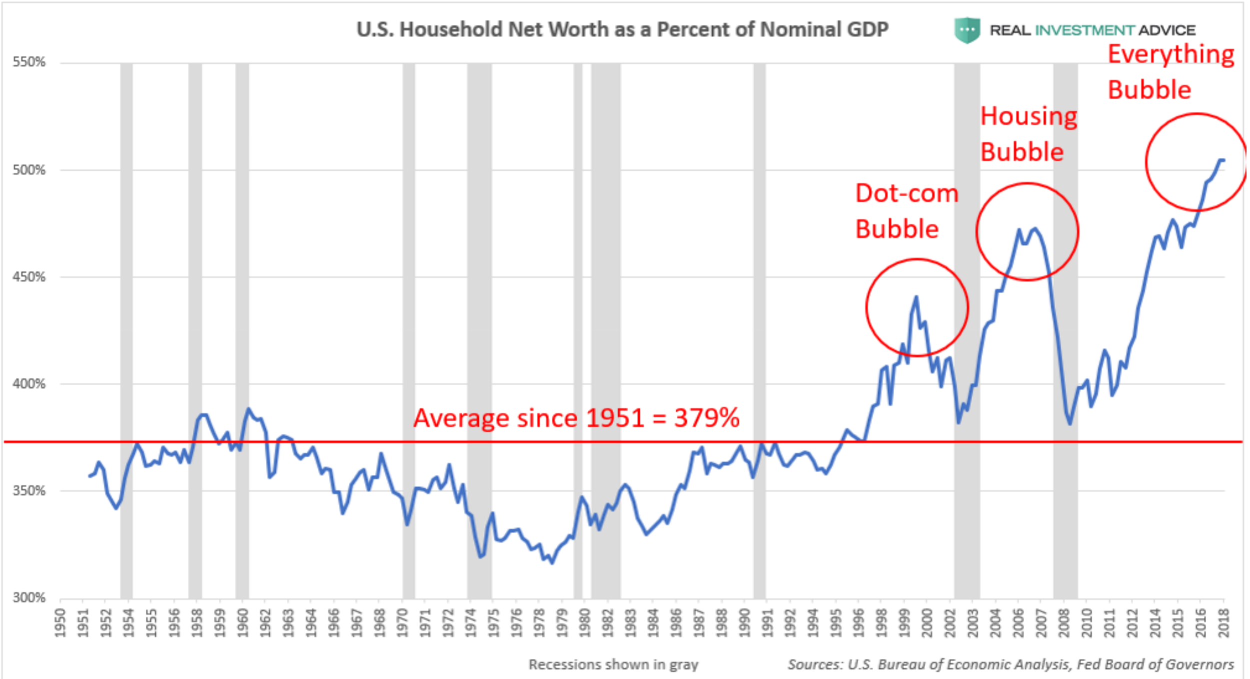
Ray Dalio, who runs the world's largest hedge fund Bridgewater, has a name for the part of the economic cycle we are entering into, and it's not pretty. Drawing parallels to the 1930's, and Japan in past two decades, the 'great sag' is approaching, and central bankers no longer have the dry powder to stimulate things the way they once did. For those that want to understand how Ray views the waves of growth and contraction, he lays it all out for you in his semi-famous 'How the Economic Machine Works'.

Riding the Waves



Dalio also pointed out that there are some serious economic fissures growing under the surface as we now live in a world where the top 10% of the 1% club has the same net worth as the bottom 90%. Determining that the wealth gap is growing, and probably won't end well, has been his drum to beat for some time. It doesn't hurt to point out that in order to be a part of inflation of assets, you need to own some assets. And that is simply not the easiest thing given how the world is structured these days.

The Rich Get Richer



Markets

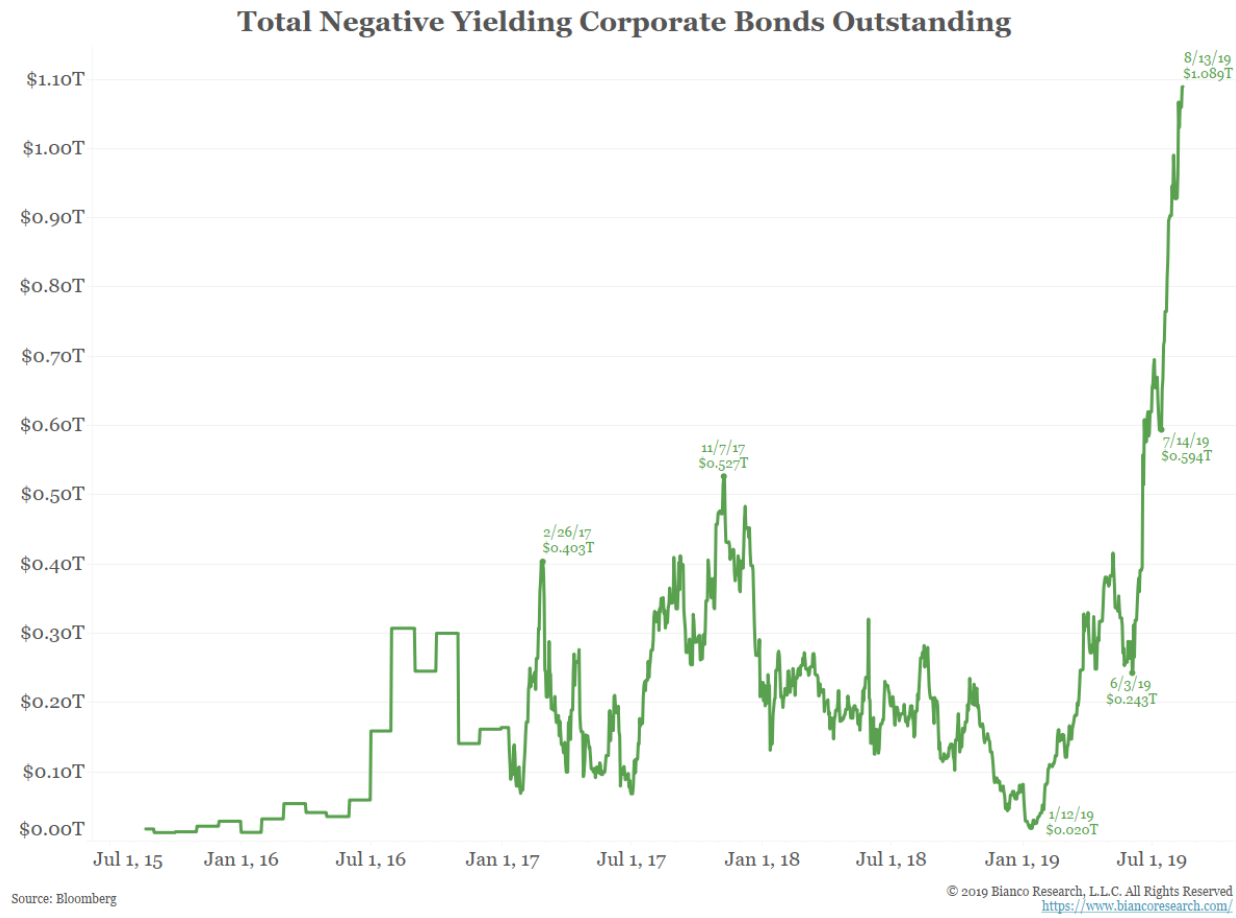
The journalistic bastion of liberalism, otherwise known as Vanity Fair, reported this week that close observers of S&P options trades now think there is some sort of 'hanky-panky' going on in the trading pits, electronic or otherwise, and its directly related to President Trump's pension for Tweeting market moving comments. While these pages are intentionally designed to be a bastion of non-partisanship, we too think there is something going on out there that can't be chalked up to efficient markets. Whether there are any shoes to drop remains to be seen.

China (Not) On the Line

Source: France42

Oaktree Capital founder, Howard Marks, penned another well thought out memo, where this time the subject was the phenomenon of negative interest rates. He entitled the piece, 'Mysterious'. In it, he not only delves into a subject that by his own admission he knew very little about, but also explains the consequences in several notable examples. Included, was an event when he sent a wire transfer to a Spanish bank to fund a deal that was supposed to close in a week. Regardless of how hard he would try, his deposit would be worth less seven days later. Normally, a depositor gets something in exchange for trusting a bank with its money. For those who lend to corporate borrowers, the situation is even worse.

No Way This is Good



If the frying pan gets too hot, will Trump jump into the fire and quit? Raymond James delves into what they consider to be an unlikely scenario given the Presidents penchant for staying in the fight. That said, it's not out of the question, as the firm notes his original intention wasn't to become the leader of the free world, but instead create interest for a new television channel to be branded Trump TV (true story). Here is what they conclude would be the narrative set about.

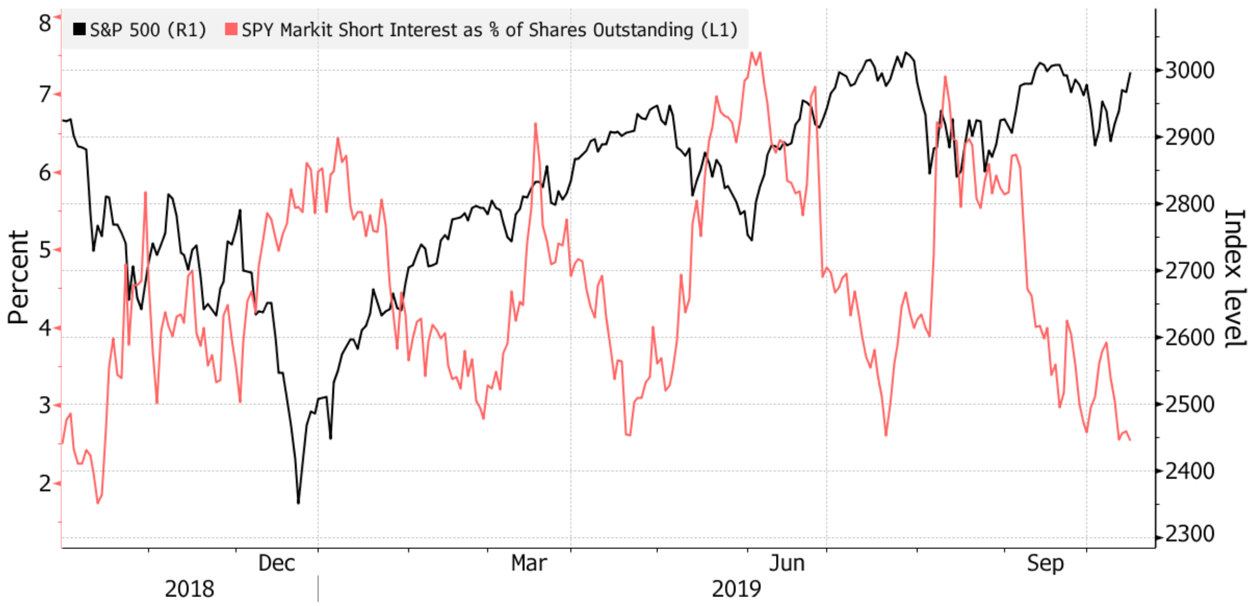
I have done everything I set out to do as President. America is great again. We have record low unemployment, the market is doing amazing, we have exited endless foreign wars, and I've stopped other countries like China from taking advantage of us in trade deals. We passed massive tax cuts and drug prices are down for the first time ever. I'm not one of these lifetime politicians. I'm ready to return to my business and spend more time with my family. This harassment of me by Democrats has really hurt Melania and my kids.

Short bets against the market have fallen off this side of the table, and are now the lowest they have been since a year ago. This reading can cut two ways. The first is there is simply a lot more optimism out there than the headlines indicate. The second, and the one where we stand, is that complacency is the name of the game these days and little in terms of downside is priced in. The man with the hot hand, Morgan Stanley's Mike Wilson, thinks so as well. He even takes it one step further by saying Friday the 11th was the near term top.

Nothing to Worry About

Complacency or Calm?

Short interest on SPY falls to the lowest in a year

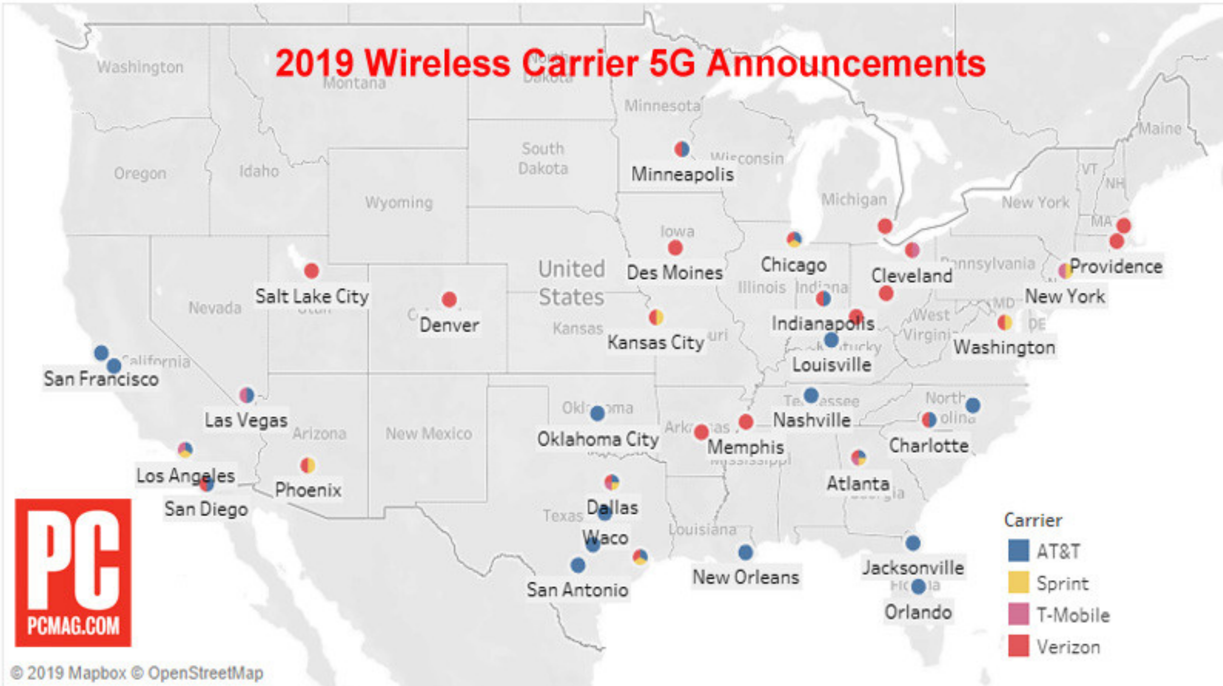


Source: IHS Markit Ltd, Bloomberg

The Bottom Up

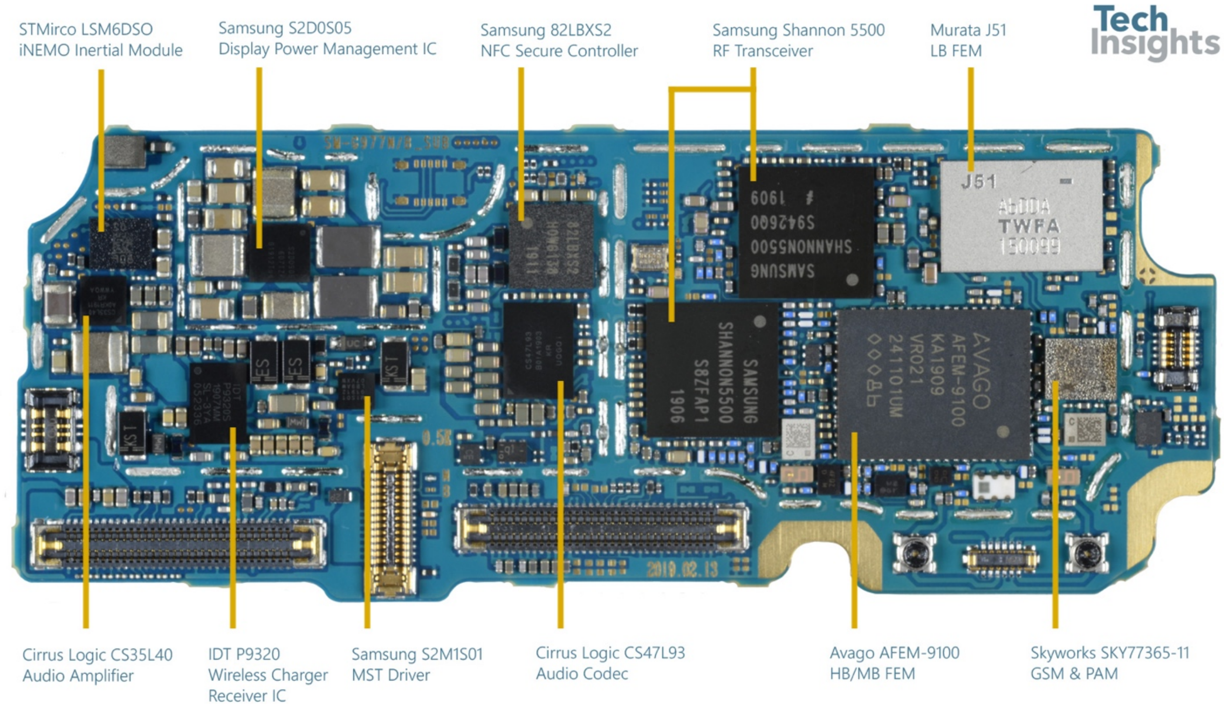
We've been skeptical of the current semiconductors rally for some time. This was partly based on the macro headwinds, and partly upon a slower than expected rollout of 5G. This week, we got a bit of a taste that perhaps our skepticism might have run its course, as network equipment maker Ericsson reported earnings that were well ahead of what Wall Street expected, this while they signaled that demand for 5G product hardware is getting drawn in, and not pushed out. Over the summer, PC Magazine wrote up a great rundown on what 5G means for consumers and equipment makers, as well as service providers, with the map below showing where the networks exist today.

No Soup for You Yet, Seattle



Our two dogs in the hunt, are Taiwan Semi from the macro perspective, and Skyworks for the device specific headwinds at Apple. In both cases we are going to need to be careful, as a further switch in the narrative will work against us. In the meantime, we take a look at the semiconductor contents of Samsung's new 5G enabled Galaxy S10. Needless to say, there is a lot of silicon on that board, from more than enough suppliers to validate further growth for the industry.

Semi Forward



Source: Samsung

Banks were early to report this quarter, and they provided the gift of stability in an otherwise nervous market. J.P. Morgan was up first, and didn't disappoint with strength in lending and investment banking. CEO Jaime Dimon, still thinks the consumer is in a position to spend with confidence. CNBC did a quick whip around the analyst community to get a feel for what the outlook appears to be going forward. They also compared notes on how Goldman Sachs surprisingly stumbled this quarter. J.P's biggest score was when they bought Bear Stearns during the financial crisis and the banks building on Madison Avenue in Manhattan.

Morgan's Headquarters in New York

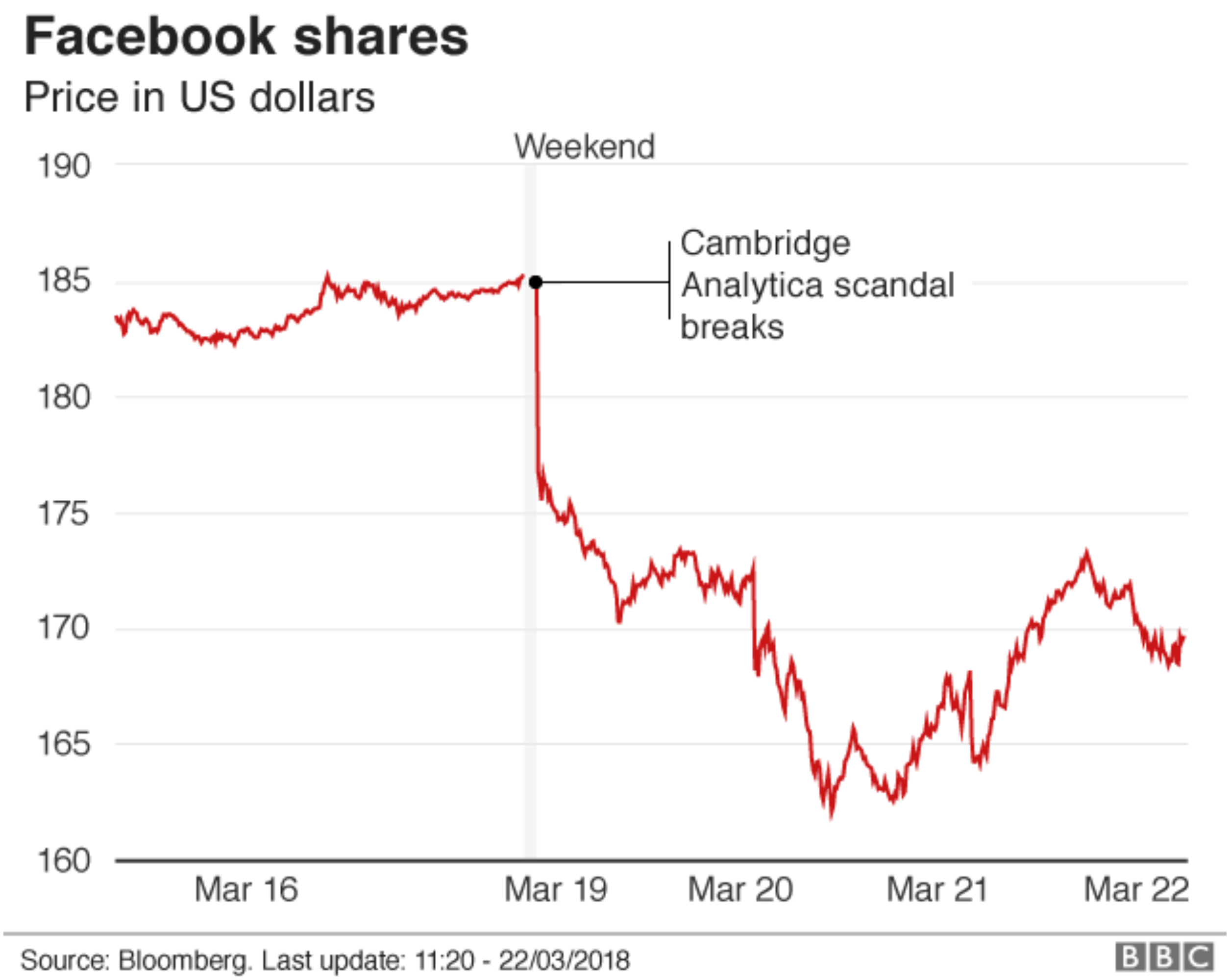
Source: Reuters

Both Bank of America and Morgan Stanley also put up numbers that conveyed confidence in the economy. BofA's third quarter came through with strength in good old fashioned lending and cost control. Morgan Stanley on the other hand pulled off good results with the help from stock and bond trading, a volatile group that has been more of a headwind than tailwind of late. The bank also continued to benefit from CEO James Gorman's' decision to de-risk the balance sheet and focus on the more stable financial advisory side of the business. The two manage a collective $2.35 billion in wealth advisory assets, more than the next five competitors combined.

Money for Something

Interbrand reports that Facebook continues to lose value while Amazon gains, at least in the eyes of the worldwide public. We mention this from the perspective that it's our belief over time that the social networks better days are behind it, and going forward the headwinds of intensified scrutiny of their business practices and the impact social media has on mental health will cause growth to slow. It's also our belief that little of this is priced in, and most of those long the stock are doing so out of lethargy and not wanting to miss out on the FANG trade. So far, we are one for one in terms of getting this right and looking forward to keeping the winning streak alive.

Down is Faster



Up and Down Wall Street

In a significant reputational blow, Highland Capital Management, a division of Dallas based Highland Capital, filed for bankruptcy this week. The move was made to protect whatever diminishing assets are left following the failure of the Highland Crusader fund in 2008. This hedge fund was on the wrong side of speculative credit and derivative positions heading into the teeth of the global financial crisis and became one of several casualties.

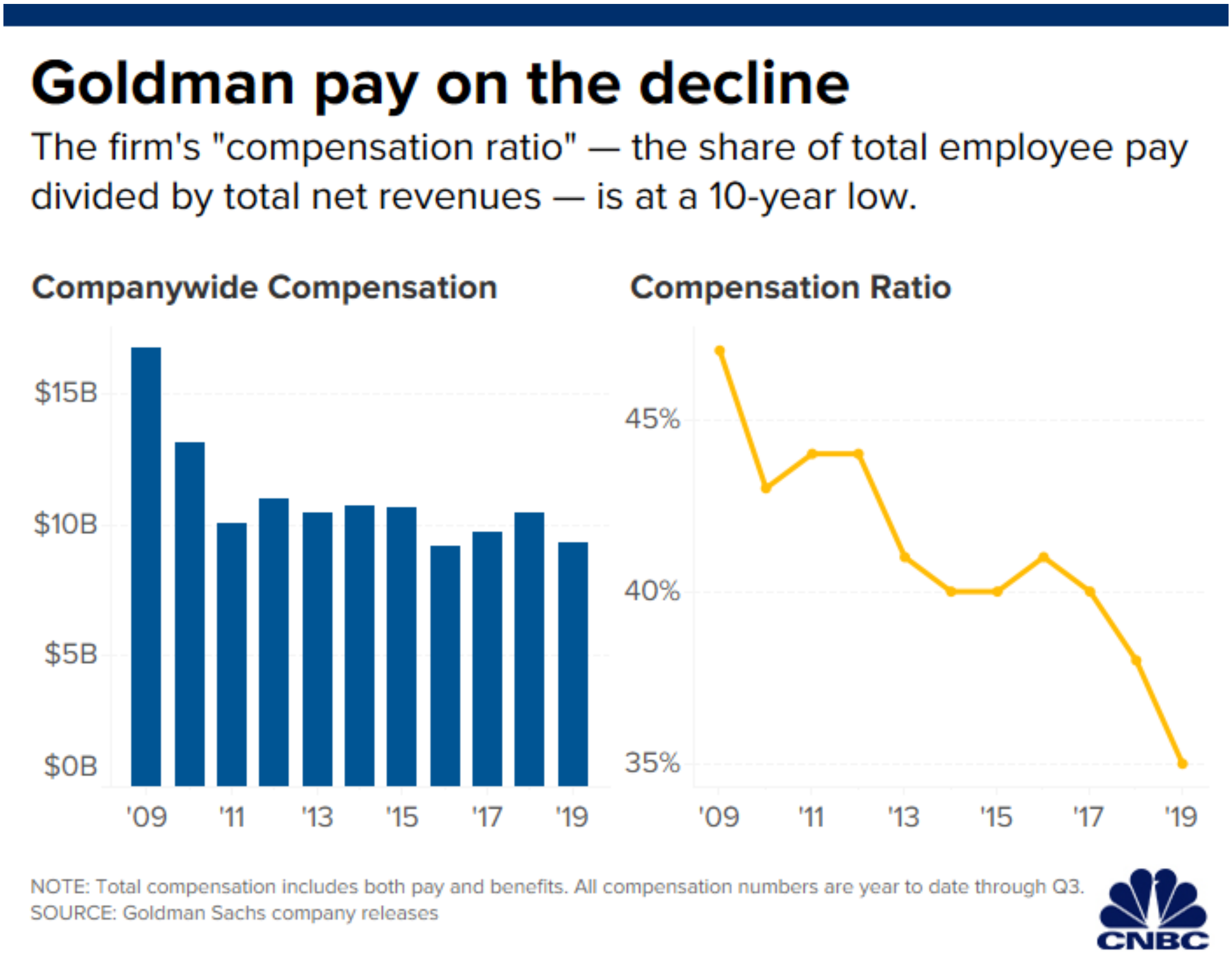
Assets Matching Liabilities

14. Estimated number of creditors	☐ 1-49 ☐ 50-99 ☐ 100-199 ■ 200-999	☐ 1,000-5,000 ☐ 5001-10,000 ☐ 10,001-25,000	☐ 25,001-50,000 ☐ 50,001-100,000 ☐ More than100,000
15. Estimated Assets	☐ $0 - $50,000 ☐ $50,001 - $100,000 ☐ $100,001 - $500,000 ☐ $500,001 - $1 million	☐ $1,000,001 - $10 million ☐ $10,000,001 - $50 million ☐ $50,000,001 - $100 million ■ $100,000,001 - $500 million	☐ $500,000,001 - $1 billion ☐ $1,000,000,001 - $10 billion ☐ $10,000,000,001 - $50 billion ☐ More than $50 billion
16. Estimated liabilities	☐ $0 - $50,000 ☐ $50,001 - $100,000 ☐ $100,001 - $500,000 ☐ $500,001 - $1 million	☐ $1,000,001 - $10 million ☐ $10,000,001 - $50 million ☐ $50,000,001 - $100 million ■ $100,000,001 - $500 million	☐ $500,000,001 - $1 billion ☐ $1,000,000,001 - $10 billion ☐ $10,000,000,001 - $50 billion ☐ More than $50 billion

Source: Highaland Capital

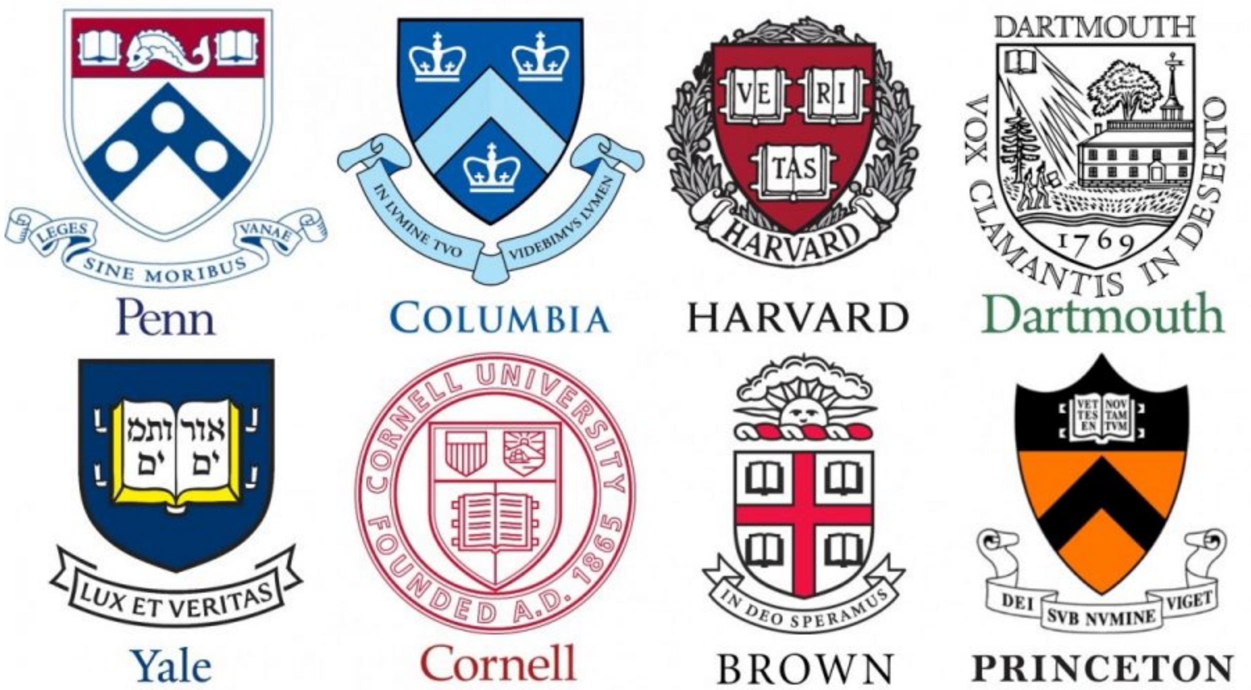
In a further sign that the good old days of yore on Wall Street are fading into the rearview mirror, Goldman Sachs reported this week that average employee compensationwas half of what it was ten years ago. At that time, those who were carrying a GS business card were taking home $525,00. Today, that number stands just shy of $250,000. As our friend, banking analyst Mike Mayo said in an interview with CNBC, this is a new era of technology in finance, and there will be 'more bots than bankers' going forward.

Tough Trend



It looks like the delta between the smarts it takes to get into an Ivy League school is getting bigger, when compared to the smarts it takes to run one of their endowments. Once again, this year returns at the multibillion dollar buckets of money institutionsunderwhelmed, as a decade long shift away from domestic equities into private equity and hedge funds continues to act as a headwind. The latter of which continue to struggle to justify their high fees. As crazy as this may sound, an off the shelf 60/40 stock and bond allocation would have served them all much better, and also cost them much less to manage.

The Ivies



Diversions

With the Washington Nationals spanking of both the Dodgers and the St. Louis Cardinals, our dreams of a glorious matchup of the former team from Brooklyn and theNew York Yankees has been blown up. The latter half of that pair could be out of contention as well by the time this publication hits the streets, as the Houston Astros are looking really strong, and Justin Vreeland will be on the mound to mop this thing up. Needless to say, the 'Natties' are, in all likelihood, the team America is rooting for over the next two weeks.

A Sweeping Success

Source: The Washington Post

The Los Angeles Times ran an interesting story this week about the growing popularity of 'Rez Golf', which as the name implies, is golf played on the hardscrabble of western Indian reservations. The first part of the story talks about how the phenomenon got its start, in the second the author described how he fell in love with it. Late last year, PBS ran a short documentary on why its relevant to those who call 'The Rez' home.

Ready for Play

Source: Indianz

As we are about a third of the way through another NFL season, and Stillwater, with a generous helping of Mentalfloss, takes a look at how each teams owners made their money, or from whom they inherited the franchise. CNBC tells you how teams make their money. And no, Jed York, just because the Niners are 5-0, doesn't mean we need to like you. Four of the team owners are female, and Commissioner Tom Goodell's wife produced a documentary on them titled 'A Lifetime of Sunday'.

Ladies of the NFL

Source: USA Today

If you have a penchant for travel, it's always a worthwhile endeavor to keep tabs on new members added to the UNESCO World Heritage Sites list. Over the summer, the organization did just that when they introduce 29 new destination as part of their annual meeting in Baku, Azerbaijan. It's nice to see Babylon make it this year as we were beginning to get a little worried.

Babylon, Iraq

Source:Wikimedia

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