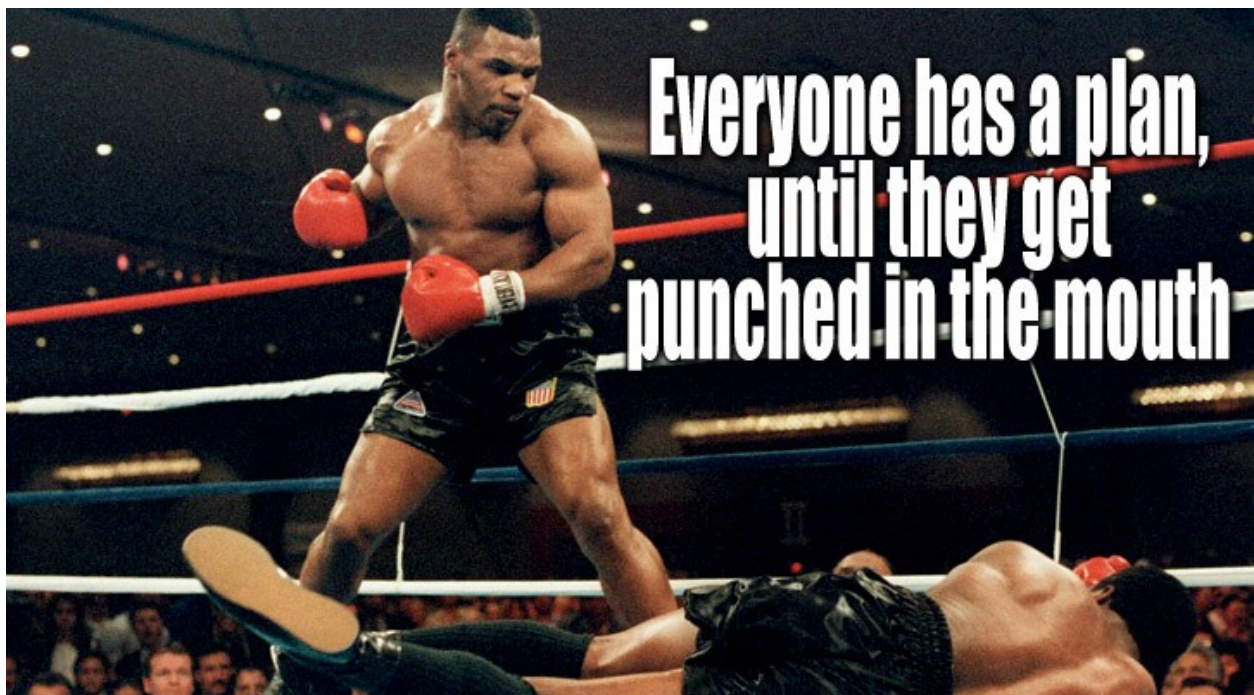


## ***Everyone Has a Plan...***

At moments like this, when the whole world seems to be turned on its head, keep your wits about you and remember what Mike Tyson once said about an opponent's plan to take down the champ. His quote, one that is now famous and used at times like this was 'everyone has a plan until they get punched in the mouth'. To be as clear as the day is long, haymakers the likes of which have never been seen before are flying, and every well laid plan is now getting tested. Thanks for the perspective, champ.

True Words Spoken



Seemingly by the hour, the world is waking up to the severity of the spread of the Covid-19, and the now apparent seizing up of credit markets. Our commentary piece took longer this week to publish for the sheer reason that everything remains so fluid.

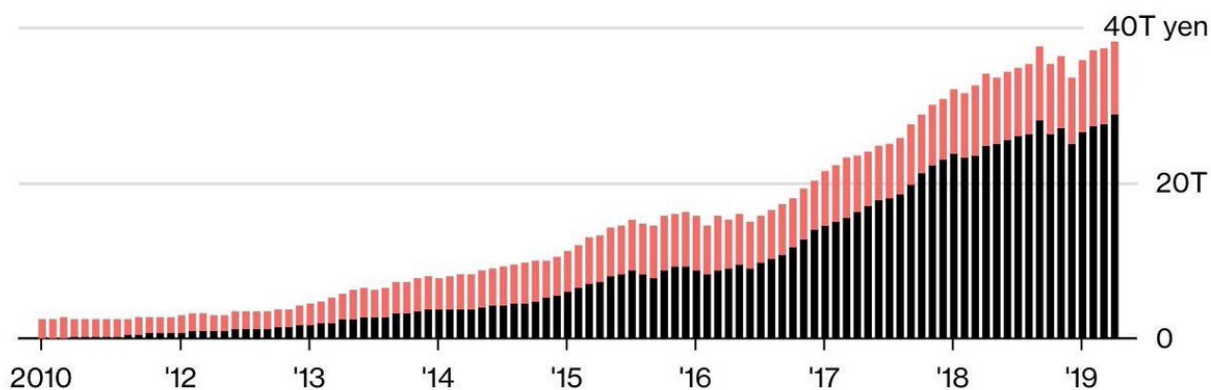
The situation has reached such a critical moment, that the Fed pulled the trigger on every bazooka it had in inventory and cut rates to zero. The only thing left, and it has become a real possibility, is for the Federal Reserve to step in and start buying equities and ETFs in the open market like the Bank of Japan has been doing.

Buy Em' Until it Hurts

## Bank of Japan: The ETF Whale

Central bank estimated to own 73% of the nation's ETF market as of end April

■ BOJ holdings ■ Rest of market



## Markets

Where do we even start when it comes to the markets right now. These are simply the most unprecedented times we most likely have ever seen. And that includes 9/11, the Global Financial Crisis, and the crash of 1987. To give you an idea of the severity of the volatility, the average move in the S&P 500 is running at 5%. That's right, the average both up and down is 500 basis points. Good luck running any sort of active money with that kind of vol. On Monday, the VIX index reached an all-time high as we took out all the gains from 2019, when the market had its worst day since the crash of '87.

## Blood in the Streets

## VIX explodes

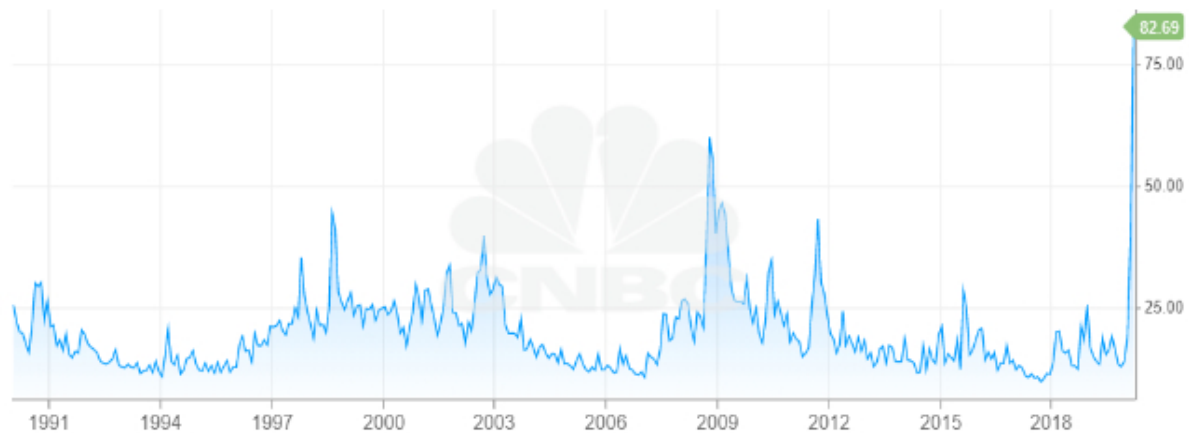
### CBOE Volatility Index (.VIX:Exchange)

USD

Last | 4:14:56 PM EDT

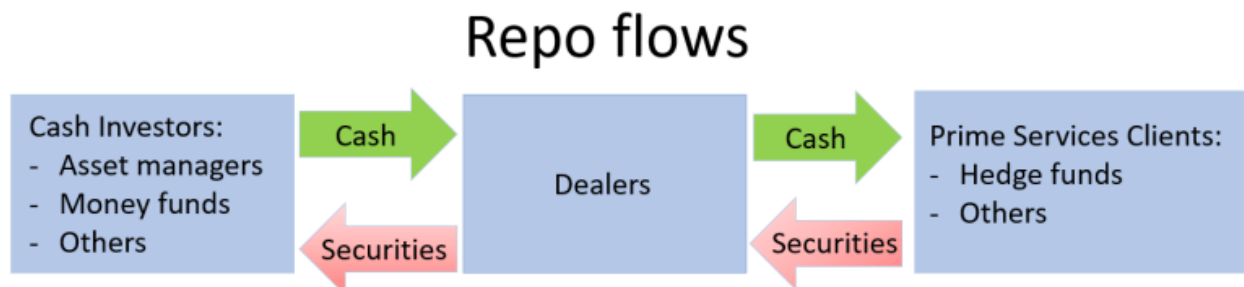
**82.69** +24.86 (42.99%)

ALL



In another sign of just how tenuous things are right now, the Federal Reserve also announced that another half a trillion was being made available for banks to swap high quality collateral for cash at 0.1% to fund operations. Known as the 'repo market', this should further help keep the wheels greased and hopefully keep the economy on the tracks. The last time this happened was in the fourth quarter of last year, and stocks took off in a massive late year rally for equities. So far there has been lighter than expected interest in showing up to the window.

## How Repos Works

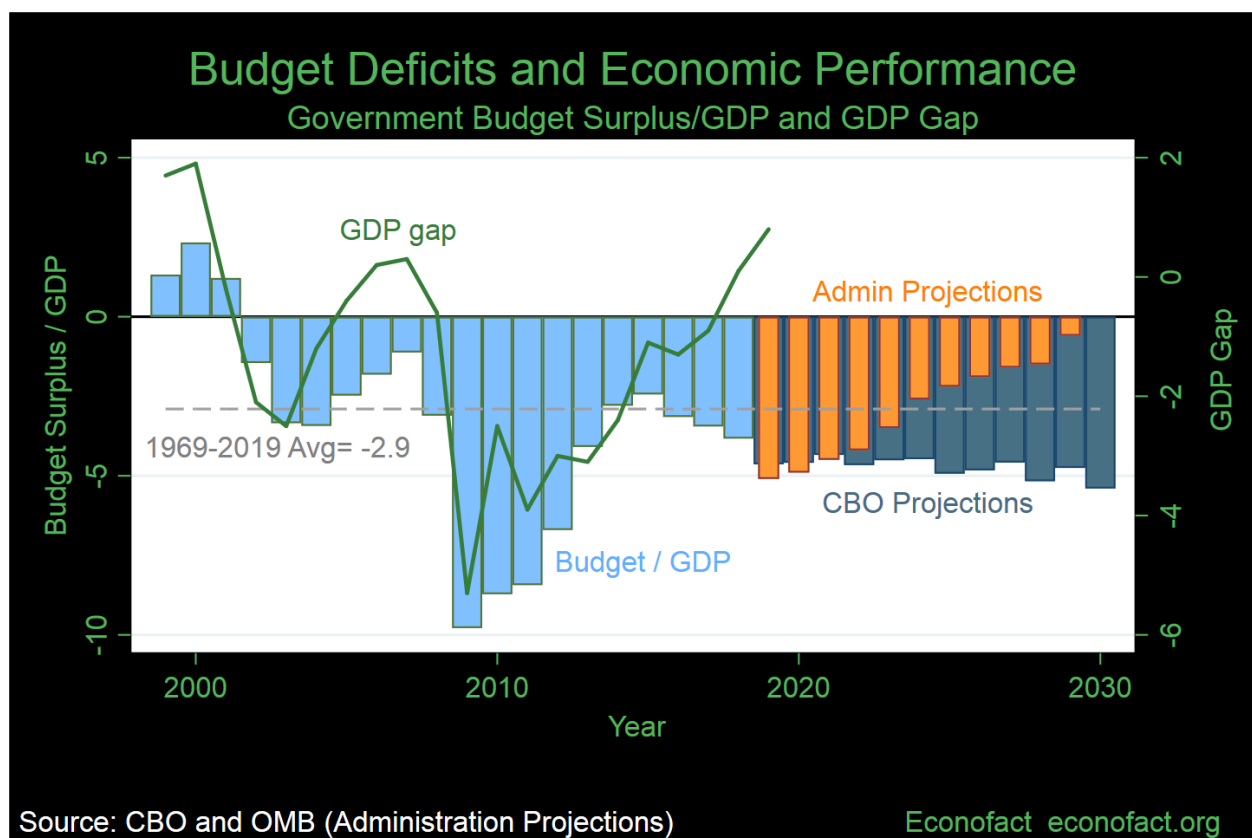


As has been pretty well analyzed, described, dissected, and debated, aside from buying equities, the Fed has shot everything it has in the arsenal. This takes us to the next option which is fiscal policy. Simply put, that's anything the President or Congress can come up with that will help stimulate the economy and/or keep it on the rails and

everything moving forward. Last Wednesday, Donald Trump brought to the table what the market thought was a watered-down version of what we needed. Then on Friday the idea of cutting payroll taxes was floated. This drew a little more excitement and the markets rallied nearly 10%, though there are still those who think it won't do much.

The problem with doing this, is it will create a huge funding problem for the ballooning federal deficit and Social Security. The former is already in a precarious place, as we need 4% GDP out to the horizon to keep it under control. DoubleLine's founder Jeffery Gundlach has been all over this subject and thinks it's a future black swan.

## Future Funding Problem

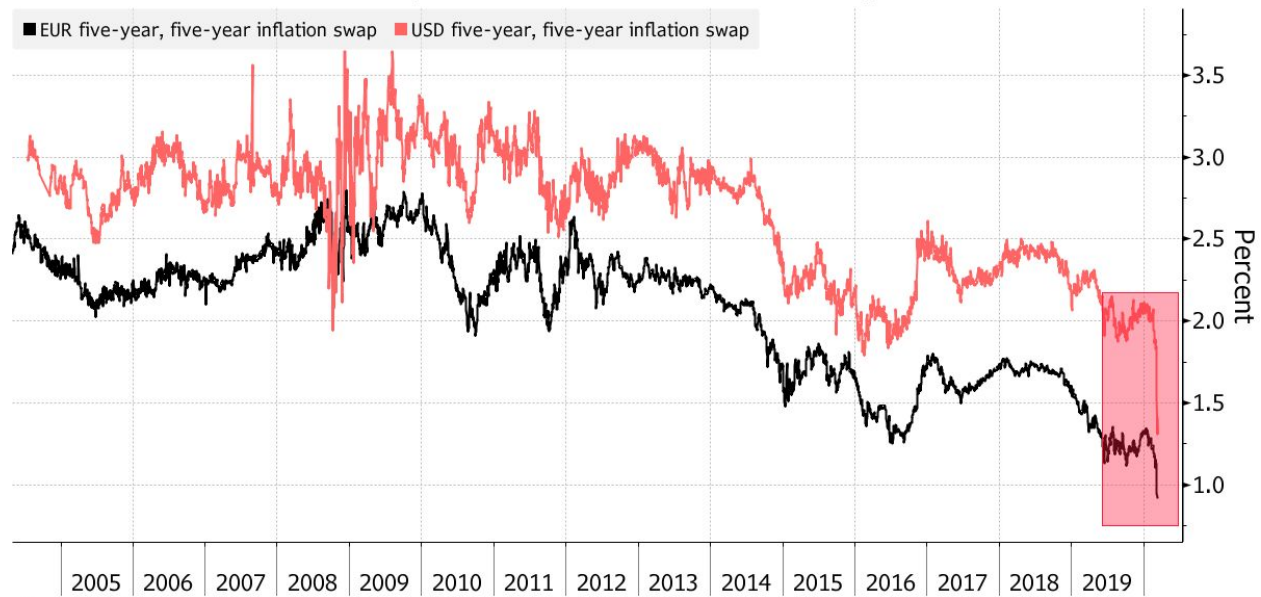


One of the primary reasons the Fed can throttle up here is that inflation expectations are now falling through the floor, and QE programs of the past never seemed to create the higher prices that bears thought they would. And now we have this...

## Deflation, Here we Come

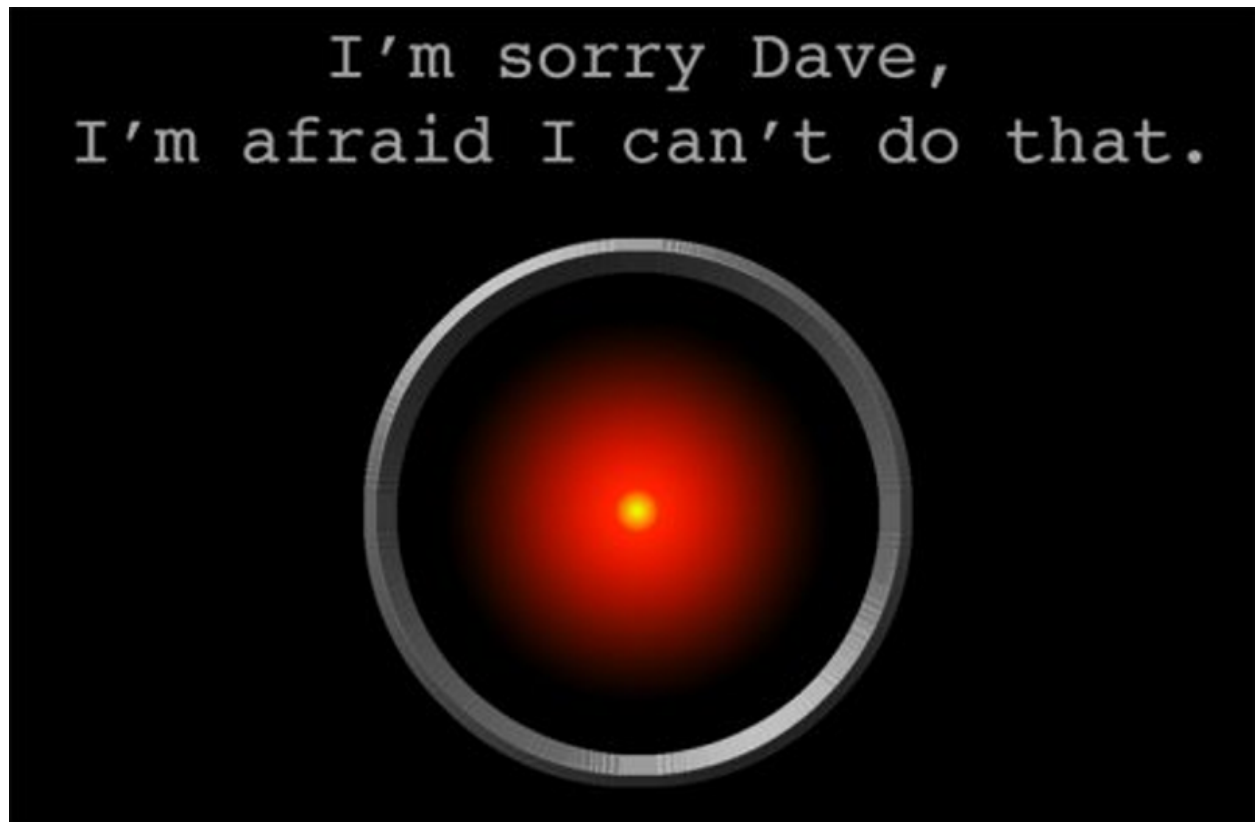
## Price Plunge

Market-derived inflation expectations in America and Europe hit record lows



Last subject we will mention is the lurking threat that too much money is now run by quants, ETFs, or by algorithms. On Tuesday the Wall Street Journal profiled Crabel Capital Management of Century City, California. By any measure, the firm has navigated this crisis well. Part of that is due to the fact they run money via quant programs that trade volatility that have nothing to do with fundamentals. The challenge, as the article points out, is that these programs tend to pile on when volume spikes or rallies take off. Point being, if you are getting seasick riding 5% up and down waves, make sure you are pointing the finger at the right robot.

HAL 9,000



## ***Credit Crisis?***

Be Afraid



We've been thinking of ways to most easily describe this moment and the best we came up with is an adaptation of 'trickle down' economics and that is 'trickle around' economics. By that we mean, that instead of the dollars flowing from the top, they are



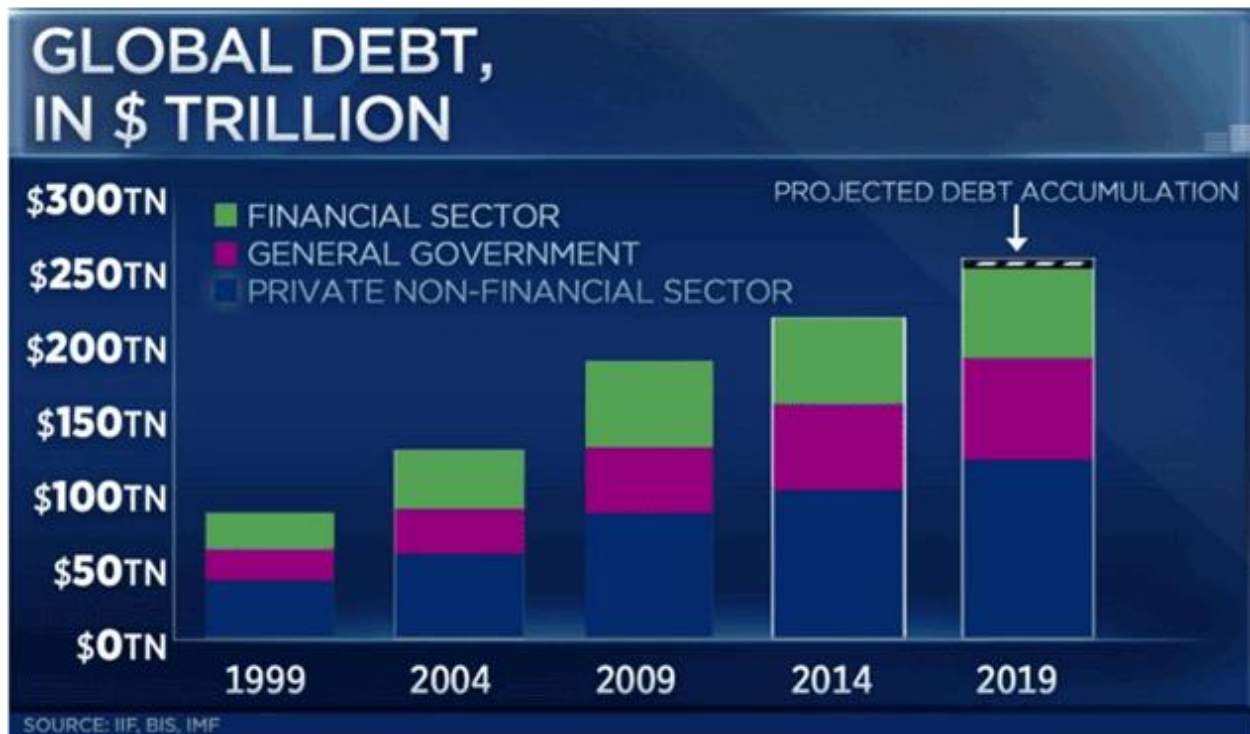
supposed to flow from all around. A full seventy percent of GDP is driven by consumer spending. Things like shutting down commerce in six counties in the San Francisco Bay Area is going to have a very material, and lasting mark on what that looks like.

## Castro Theater



Where does this falloff in the velocity of money changing hands leave corporate credit? Without sounding like Bill Walton calling a Pac-12 basketball game, in a very bad predicament. Forget equities, they won't tell you much anymore except that we are in rare times. But debt doesn't lie. And after a long binge of borrowing at low rates, there sits a huge load of corporate bonds that need cash flow while investors wait for their coupon and hope to stay at par. The ever hopeful and uplifting New York Times ran an opinion piece this week telling readers how the coronavirus was going to destroy the global economy.

## Time to Pay the Piper



Coming into this moment we already had the domestic oil & gas sector fracking companies on the ropes, and Saudi Arabia going for the kill. Now it is looking very ominous for the airlines, and those like Boeing who sell to them. This is another case of their simply being too much debt on the balance sheet and not enough cash flow to service it. The call now is that without a Federal bailout, there will be across the board bankruptcies by May. That is all of 45 days from now.

No LUV





Boeing made news last week that it was tapping every penny from its newly extended line of credit. Bottom line, they need every penny they can find right now for the balance sheet as the plane maker fights for its survival. Without diving too deep into the math, it simply doesn't look like the company is going to make it through this round in one piece. That said, it will be bailed out eventually because it has most favored 'too big to fail' status.

Bad Omen



## ***Hedge Funds***

In what can only be described as a huge hit for the hedge fund industry, Bridgewater is down a shocking 20% this year, the Financial Times reported. Last week, Bloomberg reported that other risk parity funds are suffering from recent volatility as well. None of which is good especially when leverage is involved.

Bader Omen

## Stress Test

### Stocks and bonds dropping in tandem spells trouble for risk parity



Meanwhile, European hedge fund H20 has suffered large losses across all of its funds. Some of them coming in single day down moves of as much as 15%, which calls into question the idea that these are even hedge funds to begin with, and in fact may just be funds run by people making directional bets without any protection for events like this. Which at this point, is no longer a black swan, as there have been plenty of chances to book gains assuming you had short positions in place or put out new ones when the market rallied.

Scary Bird



Not all is lost however, as some of the larger quant funds are posting some sizeable gains through mid-March. Among them is Roy Neiderhoffer's fund, which has gained 37% this year. Which is a good thing as he lost clients 28% last year. As they say in the business, easy come and easy go.

Quant King





## ***The Road Ahead***

The evaporation in equity value over the past three weeks is without a doubt, historically unmatched without comparison, in terms of speed and severity. Even in places where you thought you were safe; the market has said you weren't. We had been cautioning on the risk and valuation side and came into this crash running 30% net long. And honestly, we are now starting to run out of shorts to cover as the market is having a Wile E. Coyote moment.

Beep Beep!!!





During this time, we have participated in 50% of the downside, and on the few days the market was positive, we picked up 70% of it. Through Monday of this week, we were off half the markets 30% decline this year. There are times you thrive, and times you survive. This is without equivocation, the latter. And keep in mind, after a 15% decline, it takes you all of 17.65% to get back to even. If you are down 30%, that uphill climb back to par is 42.8%. If you like that math, and think we have a volatile road ahead and would prefer a smooth rise, we would welcome your inquiries and gladly have you as a client.

Next Stop...2,200



## ***Diversions***

Since we have entered the lockdown phase of this crisis, we thought we would provide you with a few 'greatest hits' from the movie vault that includes both the inspiring and wonderfully comical. Stream these any way you like, they are best enjoyed with a glass of fermented grape or a nice distilled cactus water. Enjoy....

### **The Shawshank Redemption**

No way to underestimate the power of this movie and the lessons it sends about the cruelties of life and how to channel inner strength to persevere. Because if the line 'get busy living, or get busy dyin' doesn't inspire you, not much will.

Red & Andy



## **The Usual Suspects**

Less inspiring, but no less entertaining, this classic from 1995 brought together a strong sleeper cast led by Kevin Spacey and a very young Benecio Del Toro. How shall we say this appropriately, you have one chance to watch if for the first time, because after it you will never be the same. Sounds like a Yogi'ism. Plus, you will go farther in life when you know how to drop an appropriately timed Keyser Soze on someone. Trust us, it's worth the effort.

## **The Goon Squad**



## Being There

Life lessons galore in one of Peter Sellers masterworks. While dated to 1979, the films messages could not be more appropriate given the state of politics these days. The plot has you following idiot savant Chance the gardener's through his exploration of the real world after having worked in the same residence for decades. Never forget, if the roots are strong, in the springtime there will be flowers.

## Chauncy Gardener





## **Cannonball Run**

Call me a fool, or a sucker for a glorious picture with one of the greatest casts ever assembled, either way this film is special. In case you haven't seen it, be prepared for Dean Martin and Sammy David Jr. dressed as priests in a red Corvette. Burt Reynolds and Dom DeLuise as paramedics looking to get Farrah Fawcett to UCLA medical center from the east coast in an ambulance. Throw in Mel Tillis, Terry Bradshaw, Rodger Moore, and Jackie Chan and you have a comedic masterpiece.

Oscar Worthy



**BURT REYNOLDS · ROGER MOORE  
FARRAH FAWCETT · DOM DELUISE**



**THE  
CANNONBALL  
RUN** *It's coast  
to coast and anything goes!*

GOLDEN HARVEST PRESENTS AN ALBERT S. RUDDY PRODUCTION · A HAL NEEDHAM FILM · "THE CANNONBALL RUN"  
Co-Starring **DEAN MARTIN · SAMMY DAVIS, JR. · ADRIENNE BARBEAU · JAMIE FARR · TERRY BRADSHAW**  
**MEL TILLIS · JACKIE CHAN · MICHAEL HUI** · Executive Producer RAYMOND CHOW · Produced by ALBERT S. RUDDY  
Written by BROCK YATES · Directed by HAL NEEDHAM · Music Conducted by AL CAPPIS

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As we sign off, we would like to remind you that this too shall pass. The sooner the better, we hope. There will be many more bumps in the road, and scary but not dangerous moments as this plays out. As it does, take a cue from country singer Dallas Wayne when he says, 'Be safe and good to one another, it's the right thing to do.' See you all in a week where we hope to be coming to you from the proper social distance and peace and quiet of Red Lodge, Montana. Because if you are going to get cabin fever, you might as well do it in a real cabin.

### Big City Set Me Loose

