April 2019

April saw the S&P 500, and NASDAQ regain all time highs. From Bespoke on Friday:

... equities sold off sharply from record highs on Wednesday afternoon after Fed Chair Powell suggested that the FOMC had no plans to cut interest rates as futures markets were implying. ...

In the last month, Jobless Claims hit a 50-year low, Q1 GDP surprised to the upside and came in at 3.2%, the stock market was at record highs, and on Friday, Non-Farm Payrolls surprised to the upside with a reading of 263K. Are there some blemishes on the landscape? Do things always look brightest at the peak? Sure, but to say the Fed must cut rates in this environment was a bit much. By the end of the week, cooler heads prevailed, and the S&P 500 finished the week less than 20 cents off its record closing high and less than ten points below its intraday record high.

Even more encouraging was the rally in the small-cap Russell 2000, which finally broke above resistance to close at its highest level since October. Traders often look to small caps for confirmation of a rally, and while we think they are often given more importance than they deserve, their outperformance this week doesn't hurt.

The importance of allowing time to work for you: https://ritholtz.com/2019/03/buy-hold-profit/

From NYT:

Trump's Dangerous Obsession With the Markets

The president is not only reading the markets as a daily measure of his success, he is also shaping policy to keep prices high.

By Ruchir Sharma

April 9, 2019

From Day 1 in the Oval Office, President Trump has shown a unique obsession with the financial markets, tweeting that high stock prices proved he was making America great again. But a new chapter opened in October, when the markets dropped sharply, and Mr. Trump began making critical presidential decisions with an eye to pushing stock prices back up.

As soon as the markets turned downward, Mr. Trump softened his hard line on Chinese trade practices, trying to quiet market fears that his tariff threats against Beijing would start a global trade war. Then he started attacking the United States Federal Reserve, saying its interest rate policies were undermining stock prices, and followed with rants about firing the chairman of the Fed, Jerome Powell.

And last week, Axios quoted a source who had spoken to Mr. Trump as saying that the president had delayed his threat to close the Mexico border out of concern over how the markets would react.

For Mr. Trump to base serious decisions about trade, monetary policy and immigration on market mood swings ensures that the zany uncertainty of his tenure will

Mr. Trump's sudden moderation on China was particularly striking because, in an otherwise mercurial career, he had remained consistent on trade. Going back to the 1980s, Mr. Trump has been accusing Asian competitors in particular of using unfair trade deals to steal America's lunch.

Moreover, Mr. Trump has been drawing broad support for his hard line on trade with China, even among his critics in Congress and in Europe. Many of them agreed that China was using state power to dominate the global information technology industry, exclude American companies from its domestic market and steal intellectual property. They were openly rooting for Mr. Trump to win on this issue, and to cut a tough deal.

Yet when the markets fell on fear of a United States-China trade war, Mr. Trump began to retreat. After taking office, his tweets on China attacked it for militarism, currency manipulation and unfair trade practices right up until the markets dropped in October. Mr. Trump's first conciliatory tweet came on Nov. 1, describing a pleasant chat about trade with President Xi Jinping, and he has been talking up their "incredible relationship" and progress in trade talks since.

By last month, amid reports that Trump advisers were calculating how big of a "stock market pop" they could expect from a trade deal, Washington insiders from both parties were worrying aloud that the president might accept any deal China would sign.

Mr. Trump, meanwhile, was executing a similar about-face on the Fed. As a candidate, he had attacked the central bank for keeping rates so low and inflating "a big fat ugly bubble" in the markets. Once he took office, Mr. Trump stopped tweeting attacks on the Fed, until November, when he began to blame the central bank for dampening market spirits with high interest rates. In recent weeks, Mr. Trump has not only fulminated about replacing Mr. Powell, he has also started considering market-friendly loyalists for seats on the Fed board of governors.

Mr. Trump's most recent market-driven U-turn appears to have come on immigration, another subject near and dear to him. So far, the stock markets have not reacted negatively to his aggressive efforts to secure funding for a border wall, including the government shutdown and the declaration of a national emergency. Nonetheless, when Mr. Trump backed off on his threat to close the southern border, the Axios source explained the president's decision this way: "It's the markets. Closing the border, the markets would plummet."

No president has shown this kind of deference. Jimmy Carter, Ronald Reagan and both Bushes mentioned the stock markets rarely and cautiously. Bill Clinton counseled against responding to their gyrations. In early 2009, Barack Obama suggested it was a good time to buy battered American stocks and was proved right when the markets hit bottom a week later. But Mr. Obama was criticized for acting as "stock picker in chief" and did not talk about stock prices again as president.

Mr. Trump is not only reading the markets as a daily measure of his success, he is also shaping policy to keep prices high. And recent market rises have rewarded him for it. After Mr. Trump turned conciliatory on China, the Fed announced it was suspending further rate increases, and stocks began climbing back toward record highs.

So who's in charge: Mr. Trump or the markets? One critical test is the United States-China trade talks, which are set to wrap up soon in a meeting between Mr. Trump and Mr. Xi. A tough agreement would help confirm that markets aren't completely dictating policy.

Even then, Mr. Trump's willingness to bend policy to please the markets is now clear — and it's risky. In recent years the stock markets have grown larger than the economy, and they are now big enough to take the economy down with them when they deflate. Policymakers are wary of poking this beast, but feeding it will only make the markets larger and more demanding.

Ruchir Sharma ... is chief global strategist at Morgan Stanley Investment Management.

Follow-ups

From the front page of April 20-21, 2019's WSJ:

States Pursue Their Own Broker-Conduct Rules

By Gabriel T. Rubin

WASHINGTON—Several states are rolling out stricter standards for investment-broker conduct, bucking industry warnings about an unwieldy patchwork of rules around the country.

The state-level rule-making, primarily in states led by Democrats, comes as the Securities and Exchange Commission moves to finish its own national conduct requirements for brokers paid by commission for investment advice. At issue are concerns about conflicts of interest, such as pay incentives that favor some investment products over others.

State regulators and Democratic lawmakers have criticized the SEC's effort, saying the commission should require brokers to meet the same standard as investment advisers (like HCM): that all decisions be made with "undivided loyalty" toward the investor.

New Jersey earlier this week took a step toward its own standards on brokerages and sales representatives, proposing a rule that would require brokers to make investment advice without considering their own financial interests. The proposal is similar to one put forward by Nevada regulators late last year, and one floated by Maryland legislators earlier this month. New York and Connecticut are also implementing versions of a fiduciary standard for some types of retirement plans and investment products. "In an ideal world, we'd have one federal standard," New Jersey Attorney General Gurbir Grewal said. "But the SEC has not stepped up."

An SEC spokeswoman declined to comment. In December Senate testimony, SEC Chairman Jay Clayton said the commission's proposal drew on fiduciary principles while recognizing the different relationships brokers and investment advisers have with their customers.

The SEC is expected to release a final rule this summer and is likely to stop short of placing a formal fiduciary responsibility for brokers. It would allow leeway for certain types of pay incentives as long as they are disclosed to a customer, while banning others, such as high-pressure sales contests.

Some Democratic state officials criticized that discrepancy and vowed to set their own standards if the SEC's final rule wasn't altered significantly.

"If the Commission does not adopt a strong and uniform fiduciary standard, Massachusetts will be forced to adopt its own fiduciary standard to protect our citizens from conflicted advice by broker-dealers," Massachusetts Secretary of the Commonwealth William F. Galvin wrote to the SEC in August.

Brokers have been generally supportive of the SEC's efforts and view the state rule-making as a potentially costly headache that could force them to limit product offerings in certain states or even pull out of them altogether. Morgan Stanley , for instance, said it could stop offering brokerage services in Nevada unless the state's rule is changed. Wells Fargo & Co., Edward Jones, Charles Schwab Corp. and others said they would pare down the investment products available to customers there. ...

For some state officials, moving individual investors away from the brokerage-commission model to a fee-based advisory system isn't an accident—it is the point of a fiduciary rule. Democratic Maryland State Sen. Jim Rosapepe, who sponsored legislation that includes a fiduciary standard, said it would absolutely push customers toward using a registered investment adviser, which he said was a more efficient way to invest.

"The fiduciary standard is going to win at some point, it's just a question of when," he said. ...

Brokers have said they may sue to block the standards from going into effect, arguing that federal rules trump state regulations. ...

Backers of a fiduciary standard have suffered setbacks in court before, most prominently when a federal appeals court threw out the Obama administration's retirement-advice rule in last June. ...

From Bloomberg:

Growth Stocks Haven't Been This Expensive Since the Dot-Com Peak

By Samuel Potter
April 12, 2019

- Global value stocks near cheapest since 2000 versus growth
- Bernstein, SocGen quants see tactical case for value rebound

For students of market history, the third month of the 21st century is infamous.

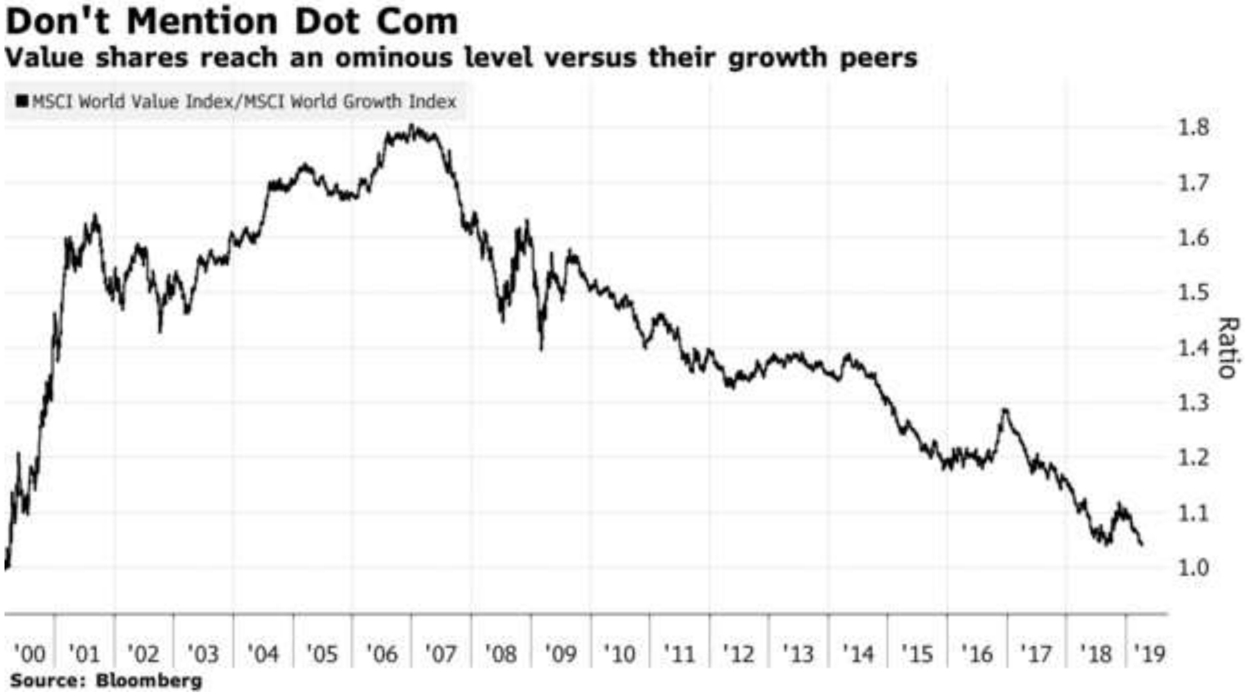
March 2000 was when the Nasdaq Composite Index marked a peak in the dot-com bubble. By the end of the year, it fell by more than 50 percent, with more losses to follow.

That month was one of the last times the world's cheapest companies looked this sickly versus their pricey peers.

As of Friday, the MSCI World Value Index was flirting with a 19-year low against its growth counterpart at less than half a basis point from its dot-com nadir. That should be a gut check for equity investors in this unloved rally, bringing with it two questions: How much crowding can growth stocks sustain? And can value shares stay this cheap?

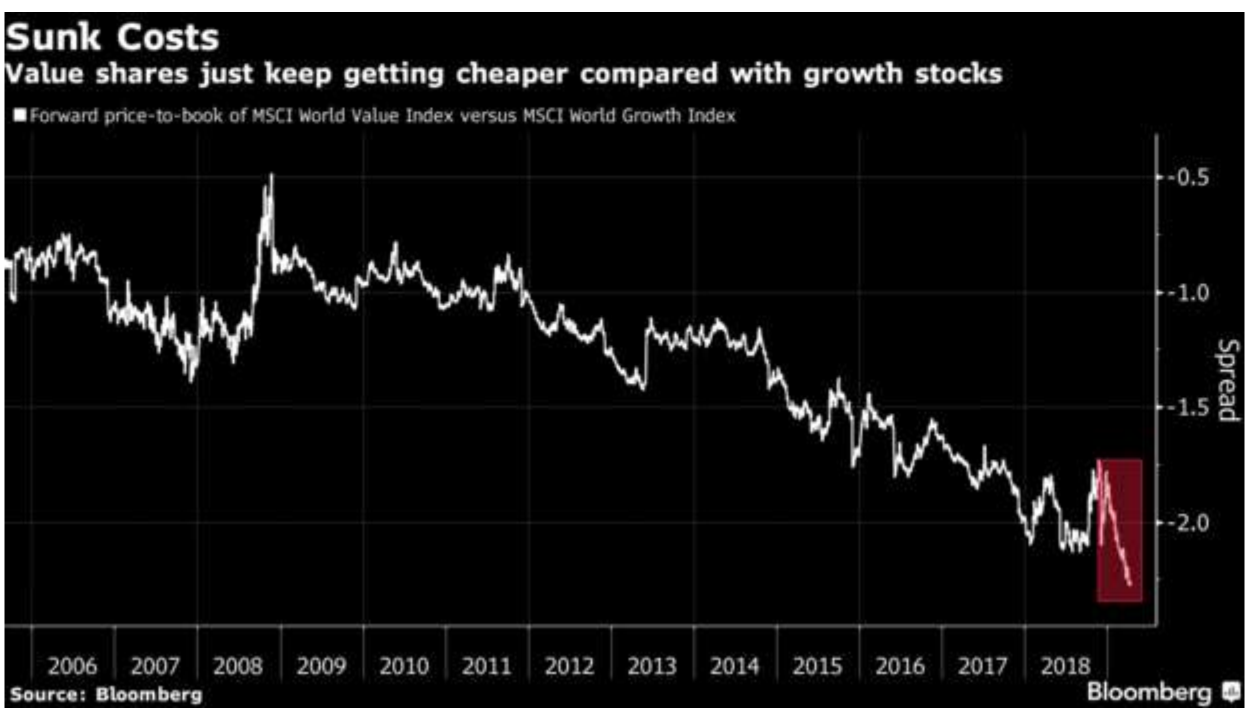
"The issue with value is that it requires a belief in the future," Markus Rosgen at Citigroup Inc. wrote in a research note on Friday. "The world will grow and in good time value will be realized. Yet that has been missing from investor mindsets. End-is-nigh discussions still dominate."

Fears for the economic outlook prompted a dovish pivot by the world's major central banks in the first quarter. Easier monetary policies punish value stocks because the group includes beaten-up industries like banks, which are more sensitive to rates, while a weaker economy makes it less likely cyclical shares like industrials will catch up. The same environment makes firms that can post reliable profits throughout the business cycle even more attractive.



That's all prompted the surging valuation gap between value and growth stocks. The monetary pivot compounded a long-term trend, of course. Cheap equities have underperformed since the eve of the global financial crisis, as investors relentlessly snubbed less reliable business models.

Rosgen at Citi is among a cohort of sell-side strategists who figure the divergence is extreme and ripe for a tentative reversal. The quantitative strategists at Societe Generale led by Andrew Lapthorne reiterated last week that they see "strong upside potential" for value shares thanks to their attractive relative valuations.



"For value to do well, economic data and earnings revisions need to be improving," Rosgen wrote. "Here the news is encouraging."

After a rough few months, the Citi Global Economic Surprise Index is showing signs of a turnaround. Friday's export and credit data from China beat expectations, raising optimism over trade and the strength of the world's second-biggest economy. On the earnings front, the number of analyst downgrades in the U.S. has eased as we head into results season. The first two big banks to report, JPMorgan Chase & Co. and Wells Fargo & Co., both beat expectations on Friday.

For Inigo Fraser-Jenkins and his team of quants at Sanford C. Bernstein, a long-term rebound of value stocks isn't in the cards. But they also see short-term opportunities emerging thanks to their current beaten-up state.

"Can value stocks rally when the yield curve is flat? Not in the long term, but that does not prevent tactical rallies, and we see a case for that," Fraser-Jenkins said.

The valuation gap flirted with these levels last year, before pulling back during the fourth quarter sell-off.

Warren Buffett in a CNBC interview published on March 29th:

"We haven't bought an initial public offering - I haven't, Charlie [Munger] hasn't - I think since 1955, I bought 100 shares of Ford (NYSE:F) when they came out...I think buying new offerings during hot periods in the market I don't think is anything that the average person should think about at all. ... you can go around making dumb bets and win. It's not something you want to take as a lifetime policy, though. I worry much more about the things that I do than the things that I don't do. I missed all kinds of opportunities in my life. You just want to make sure that you're on the side of the house when you bet rather than bet against the house."

Positions

AMZA - On 4/2 we replaced AMZA (blue line) with EPD (green line) for the 3 clients still holding this actively managed ETF. AMLP (orange line) is the 8.95 billion in Total Assets, 8.06% yielding ETF that tracks the Alerian benchmark for midstream MLPs. Morningstar's charts for ETFs do not reflect the differential in yield.

APC - On 4/25 we sold for all clients @ 72.1127 after OXY began a bidding war with CVX.

HOME - On 3/27 it was down 20.4% with 12.4 times average volume in reaction to earnings. With 6 out of the 9 analysts updating lowering their Target Price, and HOME's PEG now 1.46 we sold on 4/18 @ 22.6519 for all clients.