October 2019

On Monday the S&P 500 finally exceeded its July high, although only 8% of its component stocks hit all-time highs, a slight technical negative. With a good jobs report on Friday, the NASDAQ joined the S&P 500 at a new high, but fewer than half its components are above their 200-day moving averages, also a minor negative. The Dow is close, but Small Caps, as represented by the Russell 2000, remain 8% below their Aug. `18 high.

From Bespoke:

Bull Market Extends to 3,885 Days; 2x Longer and Stronger Than Average

Mon, Oct 28, 2019

It has been just over three months since the S&P 500 made its last all-time closing high on July 26th. If we get a close above 3,025.86 today, the current bull market will extend to 3,885 days using the standard bull market definition of a 20%+ rally that was preceded by a 20%+ decline on a closing basis. As shown in the table of post-WW2 bull markets below, this one easily ranks as the second longest and second strongest on record. We're now more than 1,000 days longer than the 1949-1956 and 1974-1980 bulls, and we're nearly 2,000 days longer than the 2002-2007 bull. We're also more than double the average bull market in terms of both length and gain. The average bull sees a gain of 154.4% over 1,700 days versus this bull's gain of 349.5% over 3,885 days.

S&P 500 Bull Markets By Length

Cycle	Start	End	% Chg	# Days
Bull	12/4/87	3/24/00	582.1%	4,494
Bull	3/9/09	10/28/19	349.5%	3,885
Bull	6/13/49	8/2/56	267.1%	2,607
Bull	10/3/74	11/28/80	125.6%	2,248
Bull	7/23/02	10/9/07	96.2%	1,904
Bull	8/12/82	8/25/87	228.8%	1,839
Bull	10/22/57	12/12/61	86.4%	1,512
Bull	6/26/62	2/9/66	79.8%	1,324
Bull	5/26/70	1/11/73	73.5%	961
Bull	10/7/66	11/29/68	48.0%	784
Bull	5/19/47	6/15/48	23.9%	393
Bull	9/21/01	1/4/02	21.4%	105
Bull	11/20/08	1/6/09	24.2%	47
		Average Bull	**154.4%**	**1,700**
		Median Bull	**86.4%**	**1,512**

Post-WW2 S&P 500 Market Cycles*

Cycle	Start	End	% Chg	# Days
Bear	5/29/46	5/19/47	-28.5%	355
Bull	5/19/47	6/15/48	23.9%	393
Bear	6/15/48	6/13/49	-20.6%	363
Bull	6/13/49	8/2/56	267.1%	2,607
Bear	8/2/56	10/22/57	-21.6%	446
Bull	10/22/57	12/12/61	86.4%	1,512
Bear	12/12/61	6/26/62	-28.0%	196
Bull	6/26/62	2/9/66	79.8%	1,324
Bear	2/9/66	10/7/66	-22.2%	240
Bull	10/7/66	11/29/68	48.0%	784
Bear	11/29/68	5/26/70	-36.1%	543
Bull	5/26/70	1/11/73	73.5%	961
Bear	1/11/73	10/3/74	-48.2%	630
Bull	10/3/74	11/28/80	125.6%	2,248
Bear	11/28/80	8/12/82	-27.1%	622
Bull	8/12/82	8/25/87	228.8%	1,839
Bear	8/25/87	12/4/87	-33.5%	101
Bull	12/4/87	3/24/00	582.1%	4,494
Bear	3/24/00	9/21/01	-36.8%	546
Bull	9/21/01	1/4/02	21.4%	105
Bear	1/4/02	7/23/02	-32.0%	200
Bull	7/23/02	10/9/07	96.2%	1,904
Bear	10/9/07	11/20/08	-51.9%	408
Bull	11/20/08	1/6/09	24.2%	47
Bear	1/6/09	3/9/09	-27.6%	62
Bull	3/9/09	10/28/19	349.5%	3,885
13 Bulls		**Average Bull**	**154.4%**	**1,700**
13 Bears		**Average Bear**	**-31.8%**	**362**

**Based on Traditional 20% Bull/Bear Markets.*

While this bull has certainly been a long one, the S&P would have to continue rallying for nearly two more years before it can take over the trophy for the longest bull market on record. From December 1987 to March 2000 (4,494 days), the index gained 582.1% without experiencing a single 20% decline on a closing basis.

From the front page of Monday's WSJ:

Hedge Fund Kings Face a Reckoning

Clients withdraw funds as portfolio managers find it harder to navigate markets and deliver returns

By Juliet Chung

Jonathon Jacobson picked stocks for three decades. He spent the 1990s at Harvard University's endowment, making winning bets on and against companies. Then he built a hedge fund, Highfields Capital Management, which made a mint in 2001 betting against Enron Corp.

Recent history hasn't been as kind. After badly trailing the market in recent years, Mr. Jacobson told investors in his $12.1 billion fund a year ago he was giving them their money back.

"I wasn't having fun," he told a group of other hedge-fund titans the next month at a Miami dinner. "How about you guys?"

Hedge-fund managers once reigned over the investment industry. The best of them accumulated huge wealth. Investment funds angled to buy pieces of their business. Clients lined up for the privilege of investing with them. The biggest endowed the arts and education and put their names on buildings.

Today, clients have withdrawn money for three straight years from hedge funds that pick stocks, either betting for or against, according to research firm HFR. That is the longest stretch of net outflows from such funds, once the growth engine of the industry, since HFR began tracking the data in 1990.

The reason isn't hard to find: They're no longer especially good at picking stocks.

Hedge funds use many strategies. Some make calls on the direction of interest rates or currencies. Some buy discounted bonds in a wager the companies that issued them will strengthen. So-called quant funds use computer models and predictive algorithms to sift vast reams of data and decide what to buy and sell.

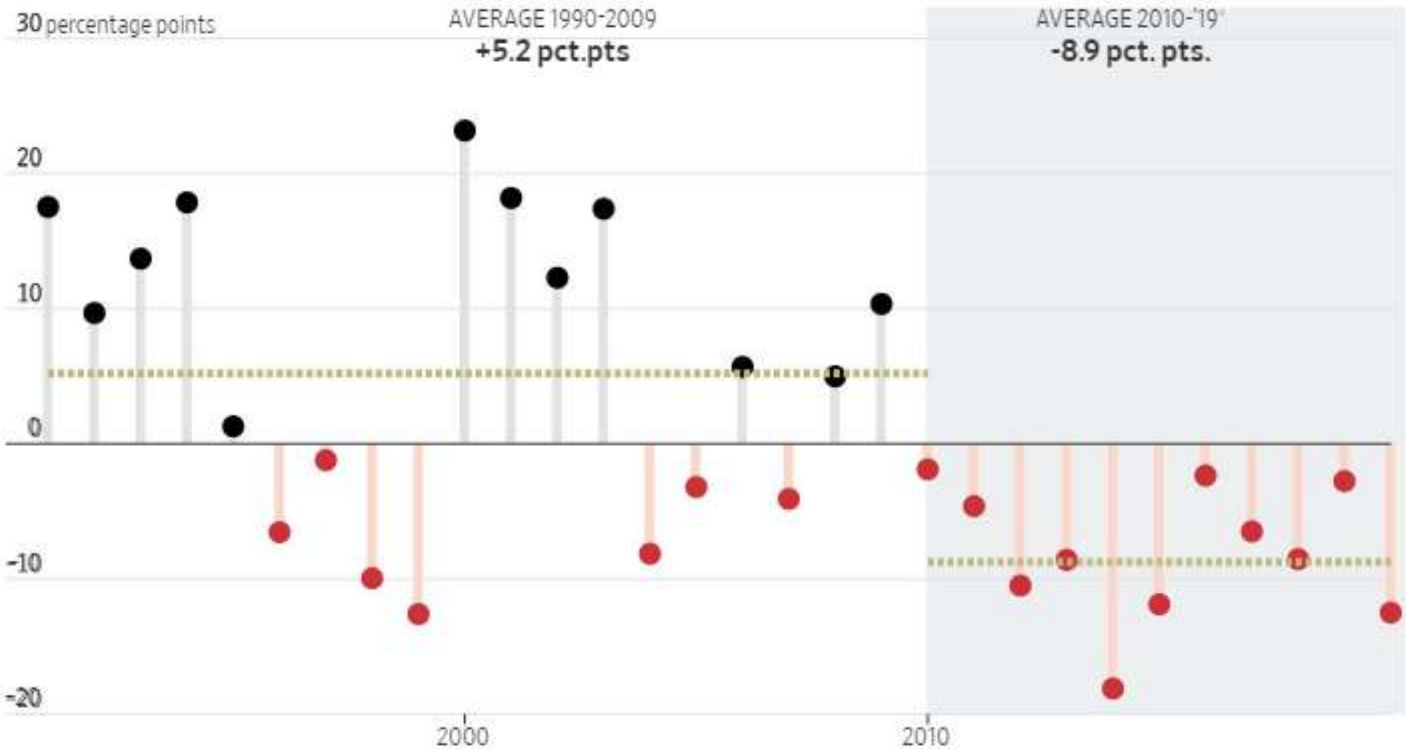
At hedge funds where human stock pickers are in charge, managers dig into corporate filings, meet with companies' managements and suppliers, parse data for insights on customer behavior, or bet on events such as mergers. Their trades are either long, wagering on a security to rise, or short, a bet it will fall.

Stock hedge funds outgunned the S&P 500's total return, meaning with dividends included, by an average of more than 5 percentage points a year from 1990 through 2009, according to an analysis of HFR data that tracks equity funds using both fundamental and quantitative strategies.

From 2010, early in a record bull run, through this September, clients have been paying those funds to trail the S&P by nearly 9 points a year, on average.

Losing Ground

Relative annual average performance of stock hedge funds compared to the total return of the S&P 500



*2019 data are through Sept. 30

Sources: WSJ analysis of HFR data tracking equity hedge funds using both fundamental and quantitative strategies and Dow Jones Market Data

"Investors are frustrated," said Greg Dowling of Fund Evaluation Group, a consulting firm that provides advice on where to invest. "Clients expect them to underperform in a raging bull market, but not by a huge degree, for years on end."

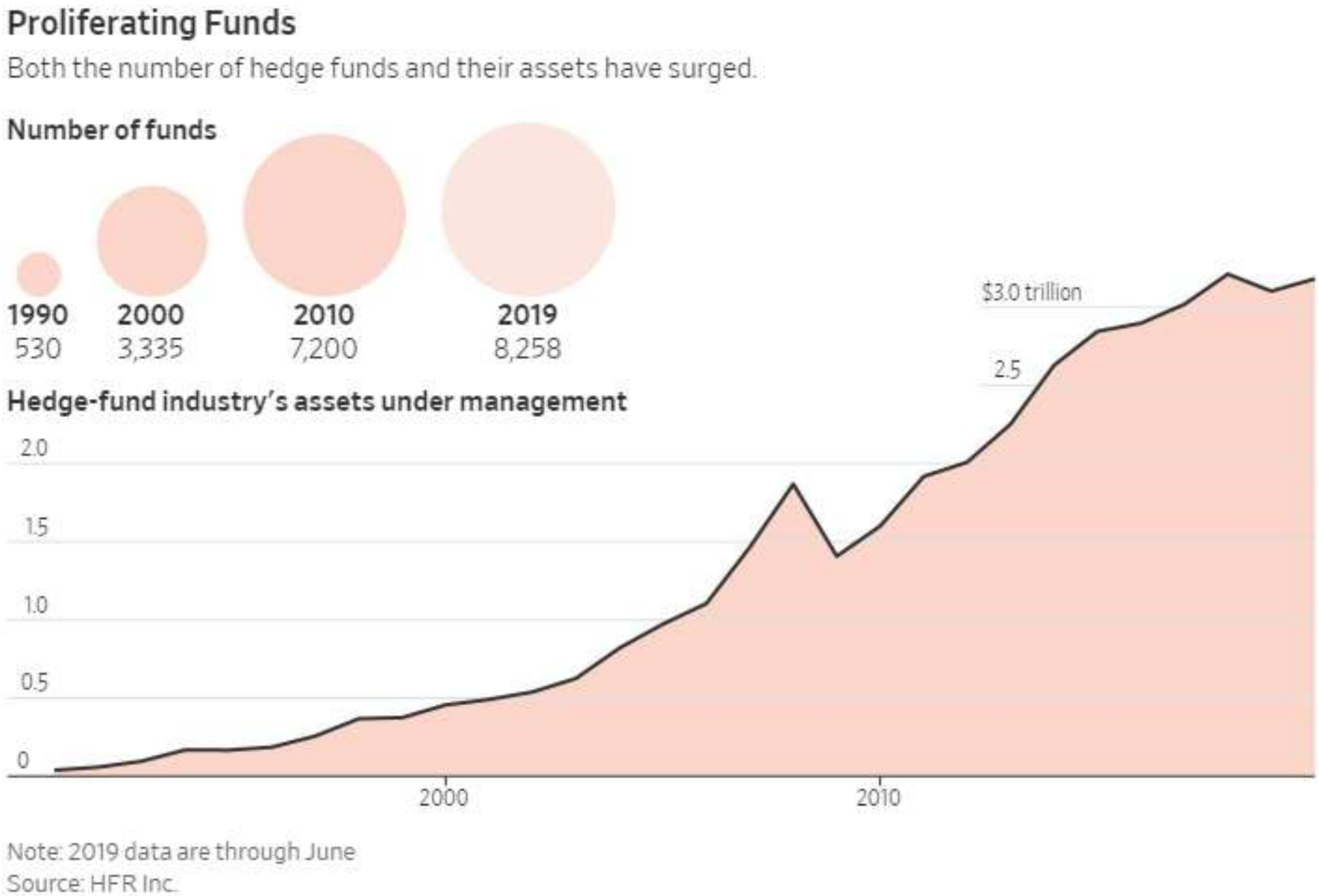
In the golden age of stock picking, hedge-fund pioneers such as Julian Robertson and Michael Steinhardt notched more than 20% gains in 1990, a year when the S&P 500 lost 3.1%. Among early hedge-fund managers was Jeffrey Vinik, a former mutual-fund star at Fidelity Investments.

Mr. Vinik closed his hedge fund in 2013 but said in January 2019 he would relaunch it and hoped to raise $3 billion in two months. He raised $465 million.

"What I learned after probably 75 meetings is the hedge-fund industry of 2019 is very different than the hedge-fund industry when I started in 1996, and it's even very different from the hedge-fund industry when I closed in 2013," Mr. Vinik said.

What changed? For one, volume. There were just 530 hedge funds in 1990, managing a total of $39 billion. Today there are more than 8,200, all trying to find winning bets for what is now a vast trove of $3.2 trillion of investor money.

For another, managers say the rise of quantitative and passive investing has distorted how stocks move and reduced the chances to profit. Quants can spot and eliminate certain mispricings of securities that once offered opportunities to stock pickers. Further complicating matters, stocks in recent years have had an increasing



tendency to move in tandem, whether on signs of a Federal Reserve rate move, a presidential tweet on trade or other events.

Low interest rates also make life tougher, by reducing interest payments short sellers earn on cash they get when they sell borrowed stock, known as "short rebates." In addition, the emergence of inexpensive financing means companies the short sellers target are less likely to go bust.

The portion of stocks traded by humans—in the market overall, not just at hedge funds—has fallen by an estimated two-thirds since the late 1990s to about 15%, according to JPMorgan Chase & Co.

Hedge funds have typically charged annual fees of 2% of invested assets and 20% of investment profits. It's a measure of their struggles that a growing number now charge less.

There's been a parade of hedge-fund shutdowns, including some that investors once clamored to get into, such as SPO Partners & Co. and Blue Ridge Capital. In each year since 2015, more hedge funds have closed down than have launched, according to HFR.

Prominent managers such as William Ackman and David Einhorn, who could readily move markets and became household names, now run a fraction of the money they used to. Mr. Einhorn's Greenlight Capital started 2019 with $2.5 billion in assets under management, versus $12 billion in 2014.

The largest investor in hedge funds, Blackstone Group, has cut back on funds where humans weigh company fundamentals. Blackstone made its call in 2015, said people familiar with the firm, in part because low interest rates were hurting funds' ability to make money from their short bets. Blackstone, which invests about $81 billion in hedge funds, shifted much of what it used to invest in fundamental stock-picking funds to quant funds.

Other investors are favoring stock-picking funds they think have a particular advantage, such as biotech-focused ones that employ scores of Ph.D.s and M.D.s, or so-called platforms that deploy several separate trading teams.

“There’s times I remind myself, these guys didn’t forget how to make money all of a sudden,” said Scott Warner of Paamco Prisma, a firm that advises on or invests $23 billion of client assets in hedge funds. “But holding your breath and hoping for change is not a strategy. The question is, ‘How are you adapting to the new reality?’ ” ...

From Jason Zweig's Oct. 4th column in the WSJ:

The Hidden Cost Of Free Trading

Freedom isn’t free, and free trades aren’t either.

Charles Schwab Corp. shook the brokerage industry this week when it said it will cut commissions to zero on Oct. 7. Schwab’s move, which followed a similar cut by Interactive Brokers Group and has already been matched by rivals TD Ameritrade Holding and E*Trade Financial, is likely to be copied by other big brokers.

You no longer will pay a few bucks in commissions to buy or sell a security at these firms. But Schwab and other brokerage firms are in business to make money, and one way they often do that is by milking clients’ cash. When you trade for free, you still pay—at a different tollbooth.

In fact, the term “brokerage” is becoming a misnomer. Firms like Schwab are more like banks than brokers. Commissions amounted to less than 7% of Schwab’s total net revenues in 2018; they were 14% in 2014.

Why take that to zero? Eradicating commissions is the logical culmination of what Schwab has been doing ever since former newsletter publisher Charles Schwab founded the company in 1973: driving down the costs of investing. Schwab’s exchange-traded funds charge as little as 0.03% in annual expenses, and the firm offers financial planning for a $30 monthly subscription (after a $300 initial planning fee).

Schwab can offer such cheap options partly because of how it handles investors’ cash. The firm automatically sweeps idle cash not into money-market mutual funds or other assets that could yield about 2% at today’s rates, but into its own bank, which pays peanuts.

As is typical in the brokerage business, Schwab puts clients’ uninvested cash—say, a dividend or interest payment—into what’s called a sweep account. It’s your money, but how much it earns isn’t always up to you.

You might be able to earn better rates. In the first half of 2019, Schwab clients moved $58 billion into money-market funds and other higher-yielding choices. But most don’t bother. Even worse, many don’t have a choice because they hold accounts that are required to keep cash at low yields in Schwab’s own bank. That has been a bonanza for the firm.

Schwab pushed $11.8 billion out of higher-yielding money-market funds into deposits at its own bank in the first half of 2019, according to the company. As of June 30, deposits at Schwab’s bank totaled $208 billion. This week, clients were earning between 0.12% and 0.55% on those balances.

Schwab isn’t alone. Across the brokerage industry, most sweep accounts pay measly rates—sometimes as little as 0.05% on a $100,000 balance.

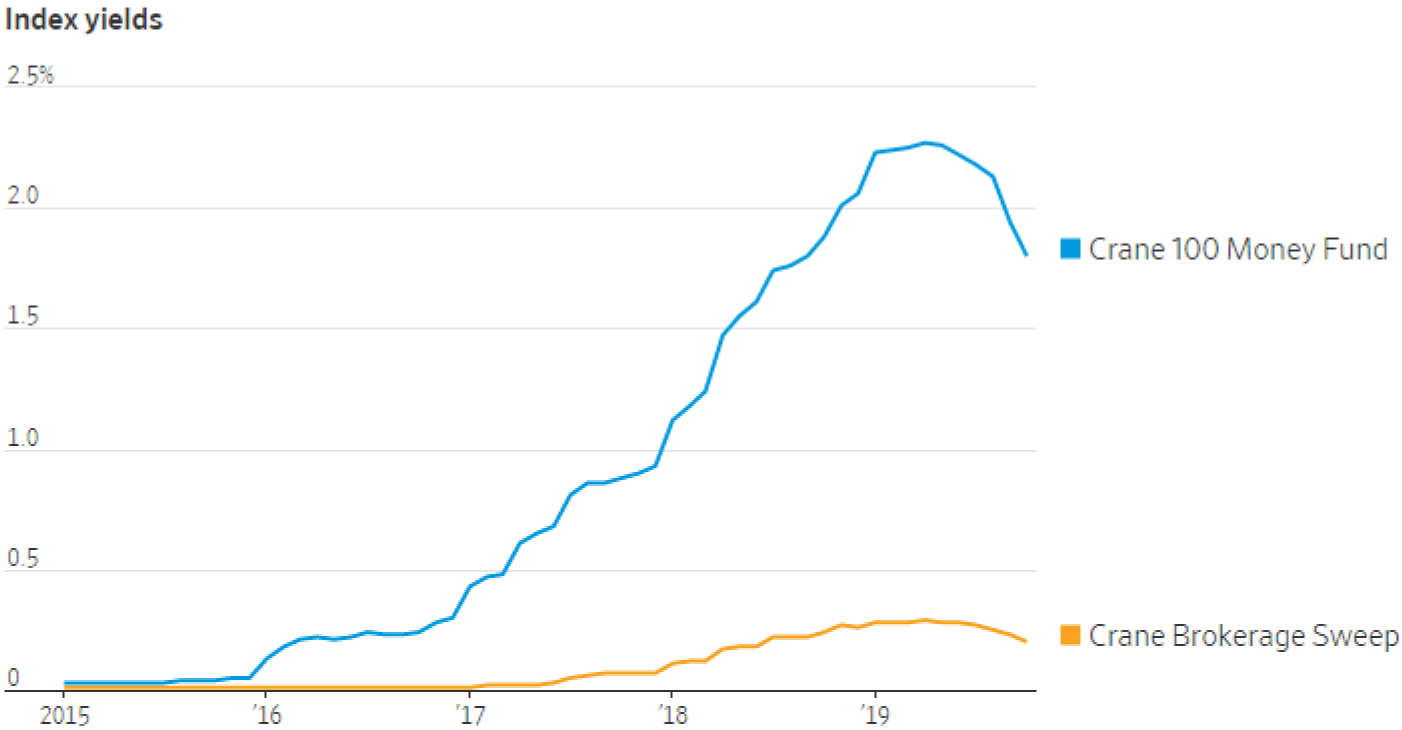
This year, with the Federal Reserve lowering interest rates, sweep yields have fallen by nearly one-third, to 0.2%, since they peaked in March, according to Crane Data, a firm in Westboro, Mass., that tracks cash accounts. Average money-fund yields shrank less, to 1.8%.

With rates falling, investors care less about what their cash is earning. “A lot of the brokers are counting on this desensitivity to rates now,” says Peter Crane, president and publisher at Crane Data.

When clients invest in Schwab Intelligent Portfolios, its roboadvisory service that offers preselected baskets of ETFs, between 6% and 30% of the money goes into cash. Schwab doesn’t use money-market funds or short-

Where Cash Is Not King

Even as the income paid out by money-market funds rose sharply and then eased down, the yield on cash in brokerage accounts has remained stubbornly low.



Note: Data through Sept. 30. Money Fund Index is seven-day yield, Brokerage Sweep Index is daily; both are annualized.
Source: Crane Data

term Treasury debt, which could earn nearly 2% at recent rates. Instead, it shunts the cash into Charles Schwab Bank, which currently pays 0.55% on the money—and then turns around and lends it out at roughly 2%.

With $41 billion in assets, those portfolios hold about $4 billion in cash. Conservatively assuming Schwab nets about 1.5% by lending out that money through its bank, the firm is making roughly $60 million a year on it. The clients, meanwhile, are earning less than $25 million.

Schwab discloses all this. The rate it pays on clients’ cash “may be higher or lower than...on comparable deposit accounts at other banks,” warns a disclosure from Schwab Intelligent Portfolios. “Schwab does not intend to negotiate for rates that seek to compete with” other cash options, adds the disclosure.

Furthermore, the document states, if you need to withdraw money from your Schwab Intelligent Portfolios account, the firm may sell some of your ETFs—potentially triggering a taxable capital gain—to restore your cash balance to its required level.

Fewer than 1% of clients hold such accounts at a 30% cash allocation, says a Schwab spokeswoman, and the average cash holding in the program is about 10%. The sale of some ETFs to return the cash allocation to its required level is no different from what happens after withdrawals from any other account that has predetermined targets for its holdings, she says.

Still, according to David Goldstone of Backend Benchmarking, a research firm in Martinsville, N.J., that tracks automated online investing services, no other roboadvisor requires clients to hold even as much as 10% in low-yielding cash.

How does Schwab reconcile forcing its clients to invest in its own bank at below-market rates with its duty to put clients' interests ahead of its own?

"We take our fiduciary duty very seriously," the company said in a statement. "Our clients who invest through Schwab Intelligent Portfolios understand the cash that will be in their portfolio before they decide to invest."

When I asked the Securities and Exchange Commission if it had any comment on how advisers treat investors' cash, Chairman Jay Clayton responded: "These are exactly the types of questions investors should be asking."

Follow-ups

From Bespoke:

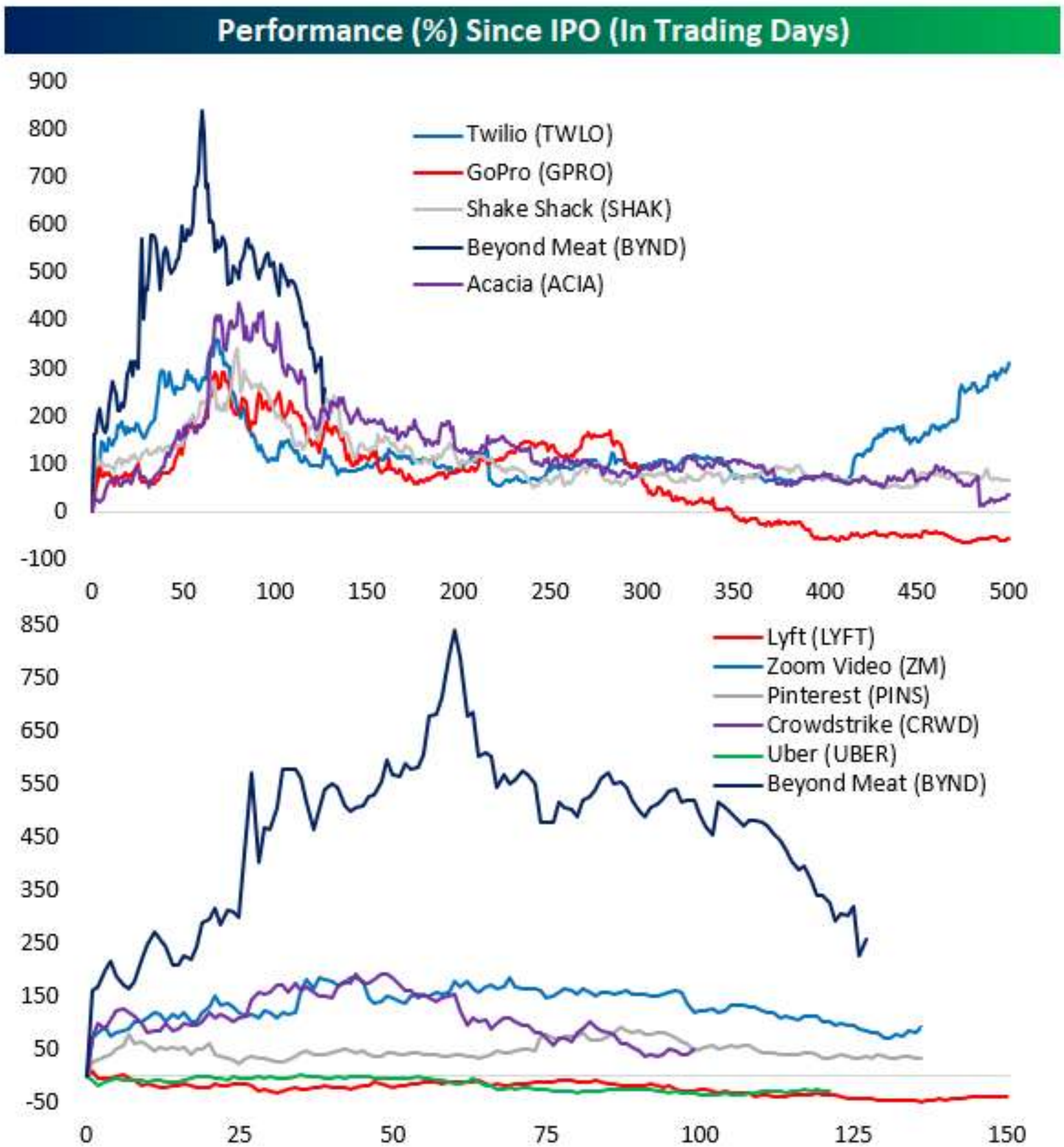
Flipping "Burgers", Flopping IPOs

Fri, Nov 1, 2019

It has been roughly six months since Beyond Meat (BYND) made its initial public offering. Although the stock was sitting on nearly an 840% gain from its IPO price at its highs back in July, BYND has come back down to Earth especially after Tuesday's 22% decline on earnings. Currently, the stock is "only" up 257% since its IPO having pared a large portion of its gains from the first few months after the IPO.

BYND has joined a number of stocks, such as Twilio (TWLO), GoPro (GPRO), Shake Shack (SHAK), and Acacia (ACIA), that have IPO'ed in the past few years, doubling or more in the first few months only to fall considerably in the times ahead. Of these, TWLO was the only one to have considerably recovered within the first 500 trading days while GoPro (GPRO) is the only one to fall below its IPO price.

Turning to some of the largest of this year's class of IPOs, while not to the same extent as BYND, Zoom Video (ZM) and Crowdstrike (CRWD) saw a similar dynamic as both more than doubled in the first 50 days but fell in the following months. On the other hand, the ride sharing giants, Lyft (LYFT) and Uber (UBER), have yet to move back above the IPO price. Although BYND has not had immunity from the classic spike and tank pattern, the stock still has dramatically outperformed other IPOs.

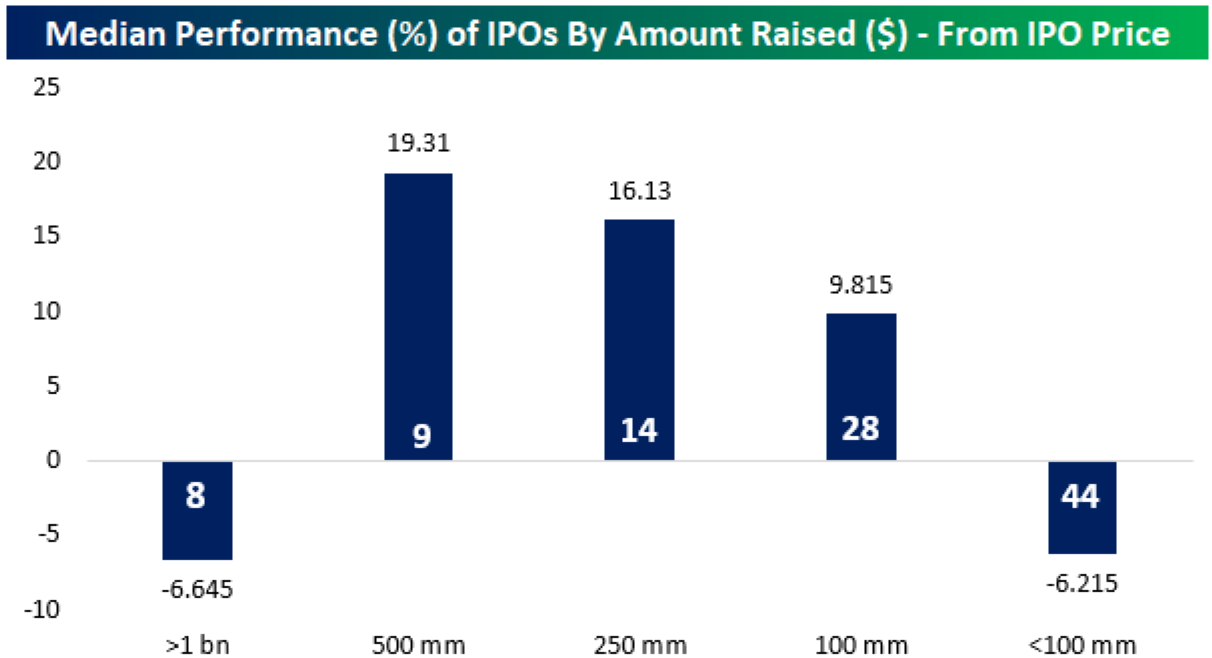


IPOs - Where Good Money Goes to Die

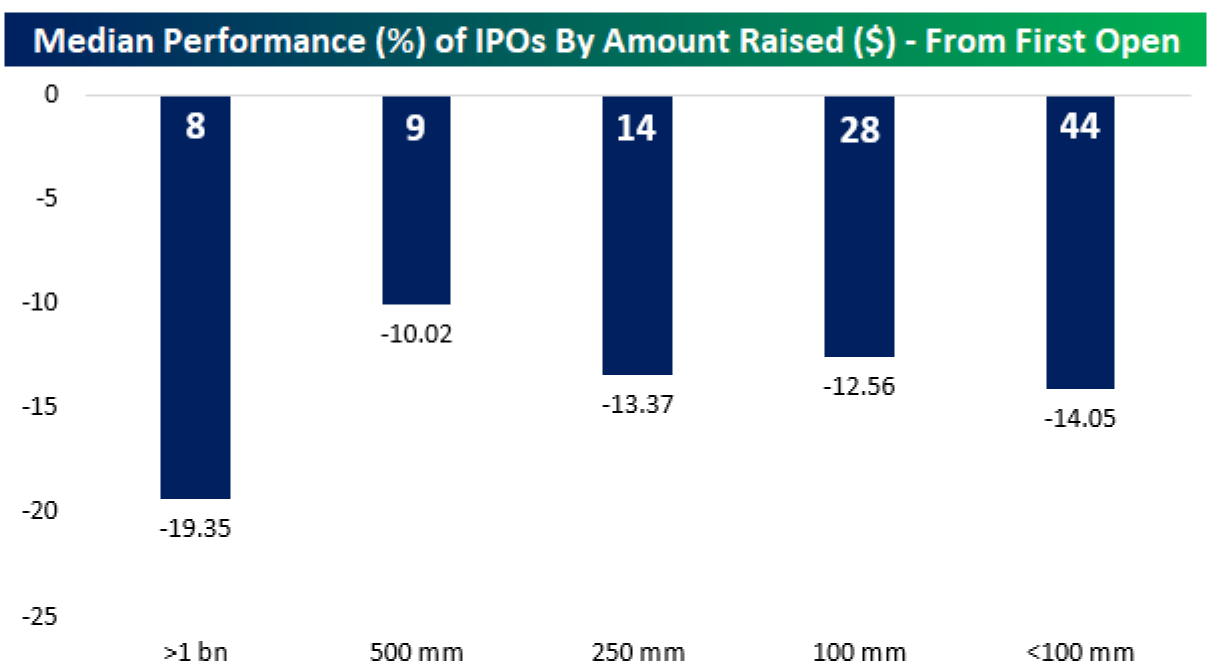
Thu, Oct 10, 2019

For an equity market that has hit all-time highs on multiple occasions during this year, one would think that investors would be salivating over IPOs for a chance to 'get in from the beginning' and bidding them higher in the process. The reality, though, is that IPOs have been one of the more challenging areas of the market to make money. The first chart below shows the median performance of US-domiciled IPOs (not including special purpose vehicles) from their IPO price so far in 2019 based on the size of their offerings. For each offering range, the number inside of the bar indicates how many IPOs were in that offering range in terms of size. Investors have had an extremely difficult time stomaching big IPOs throughout 2019. Of the eight IPO offerings of $1 billion or more, the median return from the IPO offering price has been a decline of 6.6%. IPOs in this size range include SmileDirect Club (-51%), Lyft (-46%), and Uber (-35%). Not all of these big names have been big losers, though, as both Tradeweb and Pinterest are up over 30% from their IPO price.

While really big offerings have hit the market with a thud this year, more manageable offerings in the range of $100 million up to $1 billion are generally still trading above their offering prices. It isn't until you get down to the very small, often lower-quality offerings where returns are negative again. As shown, of the 44 IPOs of less than $100 million, the median decline from the offering price has been a decline of 6.2%.



While performance hasn't been horrible for investors who got in at the IPO price, for those investors who had to wait until the IPO started trading to get in, performance has been atrocious. By this measure, every size offering range is down by a median of at least 10% with offerings of greater than $1 billion down by over 19% and offerings between $500 million and $1 billion down just 10%.



Turning to individual issues, the tables below show the best and worst-performing IPOs relative to their IPO prices. On the downside, the ten worst performing IPOs are all down over 50% from their offering price. Thankfully, most of these IPOs were small non-household Health Care names that most investors probably didn't get sucked into, but for those that did, it has been a rough road.

Ten Worst IPOs From IPO Price

			IPO	Total Amount	Performance (%)	
Ticker	Name	Sector	Date	Raised ($ mm)	Since IPO	Since First Open
GHSI	Guardion Health Sciences	Cons. Staples	4/5	5.00	-85.26	-84.49
GNLN	Greenlane Holdings	Cons. Discret.	4/17	102.00	-80.65	-88.66
SONM	Sonim Technologies	Technology	5/9	39.27	-73.91	-75.47
AXLA	Axcella Health	Health Care	5/8	71.40	-73.50	-64.95
FULC	Fulcrum Therapeutics	Health Care	7/17	72.00	-63.94	-60.21
SLGG	Super League Gaming	Comm. Svcs	2/26	24.97	-63.55	-63.55
TRVI	Trevi Therapeutics	Health Care	5/7	55.00	-59.00	-56.84
SDC	Smiledirectclub	Health Care	9/11	1345.50	-55.50	-50.19
KLDO	Kaleido Biosciences	Health Care	2/27	75.00	-53.40	-45.39
DTIL	Precision Biosciences	Health Care	3/27	126.40	-53.06	-58.28

It hasn't been all bad news for IPOs this year, though, as there have been some winners. The table below lists the ten best performing IPOs from their offering prices. Topping the list is fake meat company Beyond Meat (BTND) which has seen a gain of 471% from its IPO price in May. Other names that may be familiar to readers are Zoom Video (+104%) and Crowdstrike (+92%). While these IPOs have done very well, we would note that performance hasn't been nearly as strong for investors who couldn't get in at the IPO price. While the average gain of these ten names from the IPO price has been 136%, based on the performance where each stock first opened for trading, the average gain is half that at 68%.

Ten Best IPOs From IPO Price

			IPO	Total Amount	Performance (%)	
Ticker	Name	Sector	Date	Raised ($ mm)	Since IPO	Since First Open
BYND	Beyond Meat	Cons. Staples	5/1	240.75	470.92	210.28
PLMR	Palomar Holdings	Financials	4/16	84.45	153.47	105.51
SOLY	Soliton	Health Care	2/14	10.45	128.80	138.33
ZM	Zoom Video	Technology	4/17	748.80	104.42	13.22
TPTX	Turning Point Thera	Health Care	4/16	166.50	101.94	49.90
CRWD	Crowdstrike Holdings	Technology	6/11	612.00	92.06	2.83
NXTC	Nextcure	Health Care	5/8	75.00	90.00	83.28
HONE	Harborone Bancorp	Financials	8/13	310.00	78.73	37.59
SWAV	Shockwave Medical	Health Care	3/6	96.90	76.53	21.01
FSLY	Fastly	Technology	5/16	179.20	62.44	20.88

From "Trump’s Deficits Are an Existential Threat to Conservatism" by Philip Klein in the Oct. 29th NYT: "In July, when a caller to Rush Limbaugh expressed concern about the return of $1 trillion deficits under Mr. Trump, the radio host, who has always had his hand on the pulse of his audience, responded: “Nobody is a fiscal conservative anymore. All this talk about concern for the deficit and the budget has been bogus for as long as it’s been around.”" While we acknowledge that we, as fiscal conservatives, should be placed on the Endangered Species List, this remains one of our two biggest concerns:

The U.S. deficit hit $984 billion in 2019, soaring during Trump era

Spending increases, tax cuts and political apathy fueled the surge.

By Heather Long and Jeff Stein

Oct. 25, 2019

The U.S. government’s budget deficit ballooned to nearly $1 trillion in 2019, the Treasury Department announced Friday, as the United States’ fiscal imbalance widened for a fourth consecutive year despite a sustained run of economic growth. The deficit grew $205 billion, or 26 percent, in the past year.

The country’s worsening fiscal picture runs in sharp contrast to President Trump’s campaign promise to eliminate the federal debt within eight years. The deficit is up nearly 50 percent in the Trump era. Since taking office, Trump has endorsed big spending increases and steered most Republicans to abandon the deficit obsession they held during the Obama administration.

In 2011, the GOP-controlled House of Representatives pushed to pass a constitutional amendment that would require balanced budgets. And the Obama administration created a deficit commission looking for ways to slow the growth of government debt. But those efforts have fallen away, and budget experts believe the country will see trillion-dollar annual deficits far into the future.

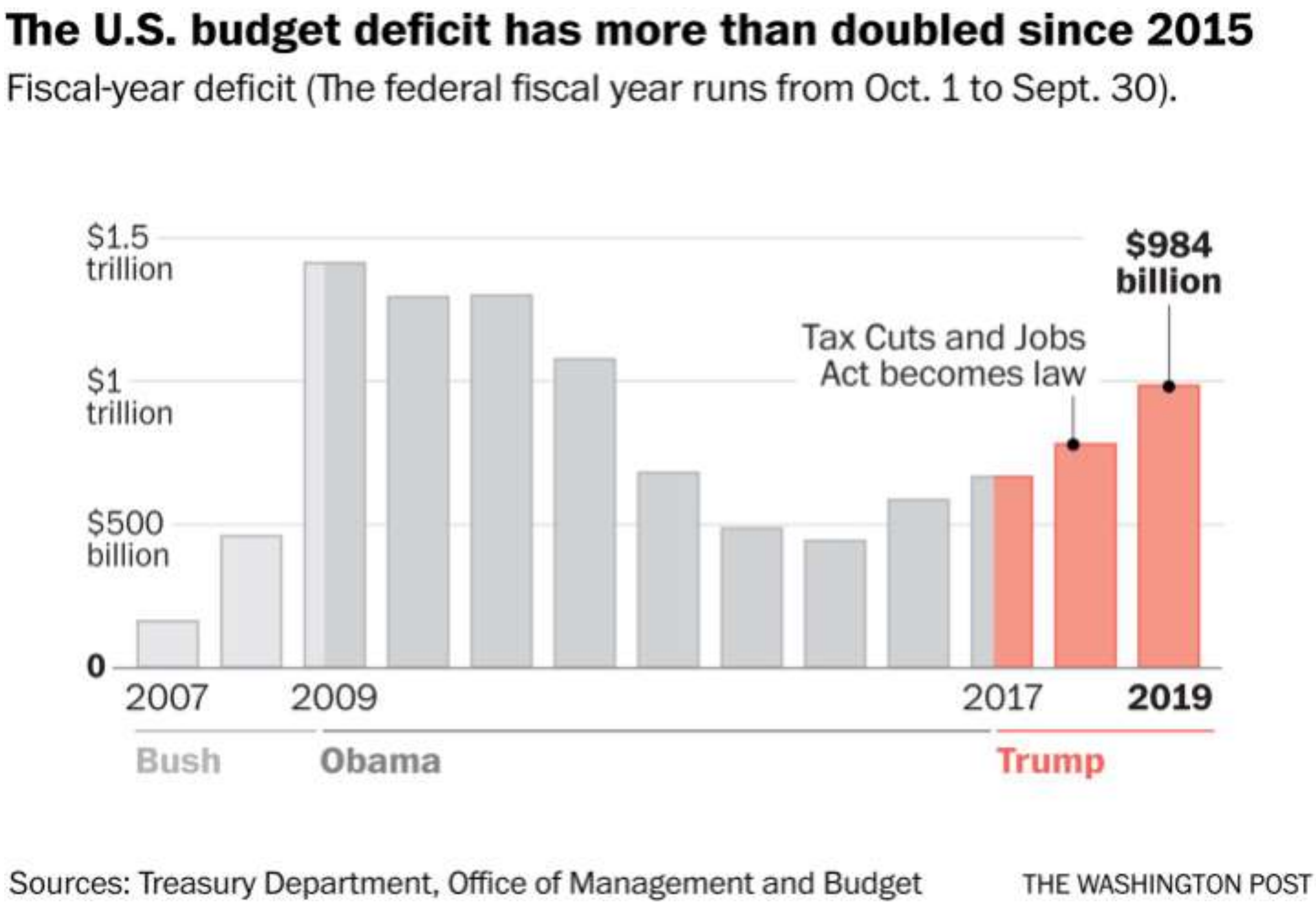
The gap between spending and revenue, referred to as the deficit, grew to $984 billion in the fiscal year that ended Sept. 30, the highest dollar amount since 2012. The government spent $4.4 trillion on numerous programs and services and brought in $3.5 trillion through taxes and other revenue.

Trump administration officials did not defend the marked deficit increase, but they cast blame on Congress for not doing more to reduce expenditures. Treasury Secretary Steven Mnuchin called on lawmakers “to cut wasteful and irresponsible spending.” But neither Trump nor Congress has done much to cut spending in recent years, with Trump repeatedly backing away from his own budget proposals. Trump has also demanded new spending on the military and for a border wall. He has recently told aides that he will focus on cutting spending if he is elected to a second term next year.

It is unusual for the government to run such a large budget deficit during a period of economic growth, because spending on unemployment and other benefits tends to contract and tax revenue often grows. But the White House and Congress have contributed to the deficit’s surge by enacting large spending increases and passing the 2017 tax cut law. The budget deficit was $665 billion in 2017.

U.S. debt is considered one of the safest investments in the world and interest rates remain low, which is why the government has been able to borrow money at cheap rates to finance the large annual deficits. But the costs are adding up. The government spent about $380 billion in interest payments on its debt last year, almost as much as the entire federal government contribution to Medicaid. ...

“This is the first time in our history that we are seeing a boom in the economy at the same time deficits are rapidly rising. It’s alarming,” said Marc Goldwein, senior policy director of the Committee for a Responsible Federal Budget, which supports reducing the deficit.



The Obama administration and Republicans in Congress enacted measures to reduce the deficit starting in 2011, and those measures — and a growing economy — led the deficit to fall by almost 50 percent. But those gains have been lost by a recent apathy among policymakers about addressing the fiscal imbalance. ...

The government recorded four straight years of budget deficits that exceeded $1 trillion around the time of the Great Recession, with the worst overrun occurring in 2009 when the deficit reached nearly 10 percent of the U.S. economy, the highest level since World War II. A growing economy and steps taken by the Obama administration and Congress shrank the deficit to 2.4 percent of the economy in 2015, but it slowly began expanding again, largely because of spending increases. In 2019, the deficit was 4.6 percent of the economy.

Budget experts also say the tax cut has led revenue to come in lower than they normally would during an economic expansion. The legislation is projected to increase the annual deficit by about $200 billion, or close to $2 trillion over 10 years when factoring in interest payments, according to the nonpartisan Congressional Budget Office.

America’s debt is hitting levels not seen since end of WWII

U.S debt as a percent of GDP

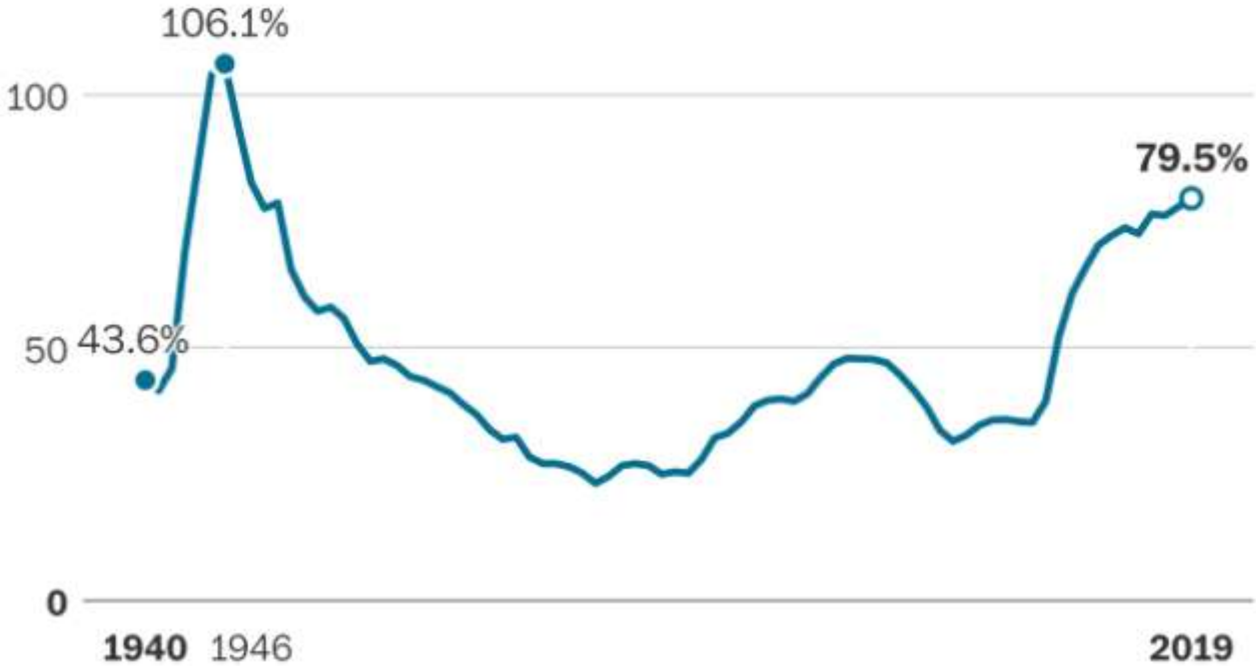


Chart shows debt held by the public.

Source: Office of Management and Budget HEATHER LONG/THE WASHINGTON POST

Tax revenue remained roughly flat the first year the law was in effect, despite economic growth of nearly 3 percent. Tax revenue was modestly higher in fiscal 2019, aided in part by a 70 percent increase in tariff revenue. White House officials said the GOP tax cuts would create so much new income tax revenue that it would offset any money lost from lower rates, but there are signs the economy is beginning to slow markedly now.

Overall spending is projected to rise by about 16 percent between 2017 and 2020, largely because of bipartisan deals struck by Congress, including a 2018 law that lifted spending limits and disaster relief funding, according to the Committee for a Responsible Federal Budget.

Military spending has risen dramatically under Trump, from about $550 billion annually to more than $700 billion in 2019, and Democrats successfully pushed for increases to other parts of the budget in exchange for their support to boost money for defense.

The leading Democratic presidential candidates are running on plans for enormous new spending programs that would likely add to the deficit, though some have said they will offset the costs with tax increases. Meanwhile, Republicans have demonstrated little appetite for raising tax revenue after dramatically slashing them in 2017.

America’s fiscal outlook could deteriorate even further should interest rates rise. The Federal Reserve has kept interest rates relatively low during this recovery, reducing the cost of borrowing and easing concerns that the deficit could trigger runaway inflation.

America’s expanding federal deficit is an anomaly among developed nations around the world. Nearly all other advanced-economy countries are on track to [see their debt shrink] as a share of their economy over the next five years, according to the International Monetary Fund. ...

Republican policymakers have made little noise about the deficit under Trump, a contrast with their dire predictions about rising red ink under President Obama.

In 2013, when federal debt totaled $16.7 trillion, Trump tweeted: “Obama is the most profligate deficit & debt spender in our nation’s history.” The federal government is now more than $22 trillion in debt, according to the White House.

Vice President Pence called the debt increases under the Obama administration “atrocious.” Mick Mulvaney, the president’s acting chief of staff, held “Spending, Debt and Deficit” town halls during the Obama administration and repeatedly criticized lawmakers of both parties for increasing the deficit, including through funding relief for Hurricane Sandy.

Positions

FLMN - On 10/11 bought for 3 clients @ 6.3.

Insider Buying:

Trade Date	No. Part	Participants	Net Sell (Shares)	Net Buy (Shares)
12/12/2018	1	Frank Brian		15,000
12/03/2018	1	HITE HEDGE ASSET		190,070
11/20/2018	1	Cohen Jonathan		12,500
11/19/2018	1	Brotman Jeffrey		15,100

From Z4 Energy Research:

The Basic Story - Eagle Ford minerals player. Truly a small cap name with but paying an annualized last quarter's dividend of $0.60 for an implied yield of 10%. Pretty simple mineral story with a focus on oil window acreage in the sweet spot of the play (they are ontrend with MGY's Karnes position). They also hold some mineral rights in Appalachia with minor amounts of natural gas production (we don't have a breakout but the EFS is in charge here). We've taken a basic look at the back half of this year and next year and with more conservative than Street production assumptions arrive at a low double digits implied yield on the 2020 number even at $45 oil. The stock is off 25% YTD and just above its all time lows.

Balance Sheet:

- 0.6x net debt to 2Q19 annualized EBITDA,
- Revolver is 35% drawn as they add acreage with debt,
- They have no senior debt.

Other Items:

- They have no capex given they are a minerals play so it's in the free cash flow and return of cash category,
- Same for LOE, none,
- Operating costs are low for their size.
- Like many in the Eagle Ford they see premium pricing for both oil and natural gas (see differentials under the Revenue section in the cheat sheet below).
- Short interest: 5% of the float is short.
- Rig count on their acreage has doubled since the start of the year (as of September); this is very strong IRR country with some of the lowest unconventional play break evens in the U.S.
- Like many non operators they note rigs on their acreage and wells in gross wells in progress; they call it line of site and it moved from 150 wells on the 1Q call to 179 on the 2Q call (a little over 1% NRI average).
- Primary operators: BP, Devon, Conoco, EOG. They say 50% of EOG, COP, and BP/DVN rigs in the Eagle Ford are running on their position.
- Management hails from Atlas (solid).
- Potential Catalyst: 4 COP operated longer laterals (Hooks Ranch wells) that should be turned in line around year end (not in the 2H19 guidance) and which have a significantly higher than normal interest for them (22.5% net revenue interest in that area with these wells coming in around 3.65% NRI).
- There's also a warrant here (FLMNW), one warrant buys one share (currently $11.38 strike, they strike can fall over time with increased dividends) with the warrant trading at $0.37 (and expiring in July 2022).

Items that may have pressured the name:

- Hedges: they don't have any but unlike some minerals companies this does not appear to be a set policy.
- 1H19 volumes came it exactly at the bottom of the guidance range; they had some one time items during the second quarter that impacted oil production,

- 2Q19 volumes were below expectations vs prior guidance (although guidance covers a 6 month period).
- 2H19 volume guidance is 5.0 to 5.5 MBOEpd vs guidance for 2Q-3Q period of 5.1 to 5.6 MBOEpd and again does not include the 4 COP wells, some of which may squeak into the calendar 2019 turn in line list.
- As with other minerals names, a portion of the production is estimated at the time of the quarterly report and trued up later. They're trying to err on the conservative side to avoid future period negative adjustments.
- Joe Allman covers the name, now at Baird. Historically he's a negative analyst led with a negative, redundant question on the last call. He may a source a piece of the shorts in the name.

Quick Model Thoughts:

- For 2H19 we get between $0.27 and $0.30 on $50 to $55 oil. Recall that 3Q just came in at $56 for the oil price average and they will come in at a premium.
- For 2020, we have assumed more modest growth than the Street. Still, at $45 oil we are at an 11% implied yield with $60 oil at 14%.

Nutshell: Interesting little mineral player with a strong implied yields. No worries with the balance sheet. Very good real estate. Big operators who are unlikely to significantly slow activity near term. Just small and likely forgotten at the moment.

IMBBY - On 10/7 bought for 1 client @ 22.6. We featured this Tobacco stock in our "Socially Responsible Investing" Worth Sharing of 10/6.