



It's Always 20/20 In The Rear-View Mirror

*"For many, it will be increasingly difficult to navigate a market dominated by the overly popular ETFs and quant (volatility-trending and risk-parity) strategies that worship at the altar of price momentum. **It is also because the 'buy the dip' mentality remains indelibly etched on the forehead of most investors and traders that the Pavlovian reaction won't die easily.** Favoring the bulls is the diminished number of publicly held companies outstanding (from more than 7,600 in 2000 to 3,800 in 2017), a 17% reduction in the float of the remaining companies via corporate buybacks, and still-abundant liquidity. And on top of this, as previously mentioned, is the market's participants confidence in buying the dips." - Kass Diary, The Bull Wont Die Easily (November, 2017)*

In trying to understand the relentless "Bull Market" advance since the Trump Election fourteen months ago I am reminded of what I wrote above in November, 2017. These words were underscored in Jim "El Capitan" Cramer's "Four Reasons Stocks Keep Going Up," written at the

end of yesterday's trading session, in which he discusses the important structural changes that have led to the popularity of passive investing (ETFs) and in the share count drop caused by a near decade of aggressive corporate buybacks. Of course there are numerous other reasons (*some Jim details further*) **like the employment of large liquidity infusions from central bankers around the world, optimism about the cut in corporate taxes, the reductions of business regulations (around the fringe), sustained lower interest rates, etc.** As I have also written, investment vision is always 20/20 when viewed in the rear view mirror. These past observations don't really help us project the future -- though I did touch on some of my concerns in yesterday's opening missive, "*Blinded By a Sense of History*" (with some updates in parentheses):

"It is a mania shared by philosophers of all ages to deny what exists and to explain what does not exist." - Jean-Jacques Rousseau

I have no clue how long it will continue:

** What I am certain about is that liquidity, which has buoyed our markets for years, is starting to be reduced. (Central Bankers are reversing course and beginning to contract their balance sheets) * What I am fairly certain about is that we are at sentiment and valuation extremes -- at least based on history. (And every day these measures grow more stretched) * Interest rates are likely headed higher, posing -- at some point -- a potential risk and alternative to stocks. (The ten year US note yield rose above 2.50% this morning) * I expect no further major legislative initiatives coming out of Washington, D.C. -- specifically on the infrastructure front -- and a further deterioration in the relationship between the Republicans and Democrats as we move toward key midterm elections. (My expectation is that the House goes Democrat while the Senate stays Republican.) * As to the Administration, their belief appears to be that the benefit of world leadership is not worth the costs -- which runs the risk of a policy mistake in the year ahead. * As well, though markets have not been yet unnerved even with the White House having gotten bitten by a Wolff this past week, there exists the possibility that the Special Counsel's activities could be market unfriendly. * And I am of the view that the earnings and economic growth expectations will, once again, be disappointing in 2018-19. (Earnings revisions higher have been material (in large measure from tax cuts) but I see mid year as a pivot point of slowing, not accelerating growth)*

The markets seem to be moving back to being one with more concentrated leadership -- as technology and the FAANGs (*a large percent of the S&P Index*) have regained their strength. Small caps, supposed tax cut beneficiaries, are lagging. **Again, historically these are not positive signposts but it can continue, I have learned, far longer than I anticipated.** The speculation in cryptocurrencies and blockchain and penny stocks is yet another thin reed indicator of a mature Bull. **And so is the self confidence and hubris seen in the business media.** Risk assets, like stocks, are called risk assets because they have risk -- though you wouldn't know it from the recent action in which fear and doubt has left the Exchanges. **But, wrong is wrong -- and I continue to see ghosts that few market participants are viewing, blinded by a sense of history.** My strategy, given that the markets have clearly moved so much higher than my baseline expectations -- is to become more trading oriented and to maintain high cash levels. As described in my Diary, **I see few longs that meet my standards of purchase.** As the market moves almost parabolically, I have recently begun to more aggressively short strength while keeping my stops fairly tight. (*Day or days trades.*) Recently, with the exception of the last day of the year in which I profited, this has been a losing proposition. **Wash, rinse, repeat.** My view through the windshield (and the future) has been dramatically worse than my view through the rear view mirror (and the past) as stocks have marched ever higher without the sign of any meaningful pause. **While Grandma Koufax used to say, "Doug, matzah doesn't grow to the sky," the investment trees are like redwoods these days.**