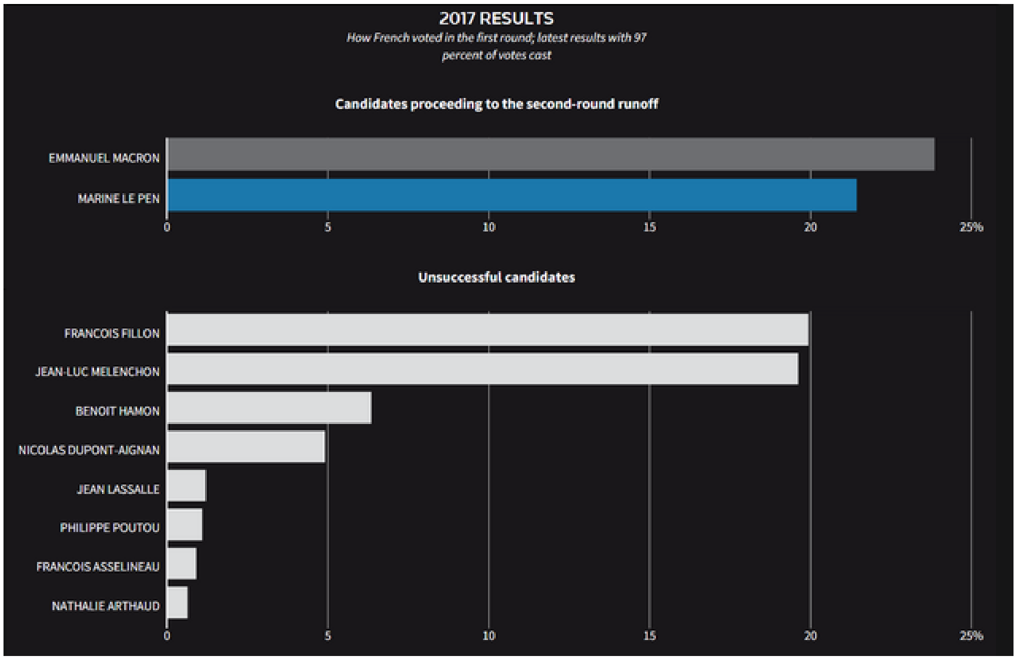
MARKET BRIEF

EUphoria



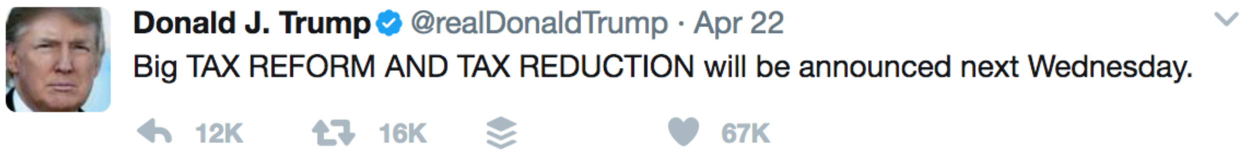
It looks like our base case for French elections which we covered in last month's *MIR* may be playing out. Marine Le Pen and Emmanuel Macron took the majority of votes and will face off in the second round on May 7th. This marks the first time in the history of France's 5th Republic that a main party candidate will not be running in the second round — another sign of the interesting times we live in.

The betting markets now heavily favor Macron. It's assumed he'll pick up Fillon and Hamon voters to handily defeat the more divisive Le Pen. But betting markets can get things horribly wrong (as we saw in the last two big electoral events) and when you combine that fact with a record number of undecided French voters, it's dangerous to have anything close to strong conviction in the outcome.

Markets have gapped higher on the news. The euro is up and the dollar is down. European and US indices are up a good deal and bond futures are down much lower... looks like we took profits on our bond trade just in time.

It looks like markets have been able to hold these jumps into today's close. This could mark the beginning of a significant thrust higher in the broader indices. Market sentiment turned notably bearish over the last few weeks even though price action remained resilient. A turnaround in bearish sentiment will be supportive if markets can maintain this advance. Also, just an interesting side note, but apparently Schwab saw the most new accounts opened with them in Q1 since the second quarter of 2000. Looks like retail is finally making its way back into the market.

There's a number of other events this coming week that could either derail markets or act as a narrative boost to the reflation trade. Trump tweeted this:

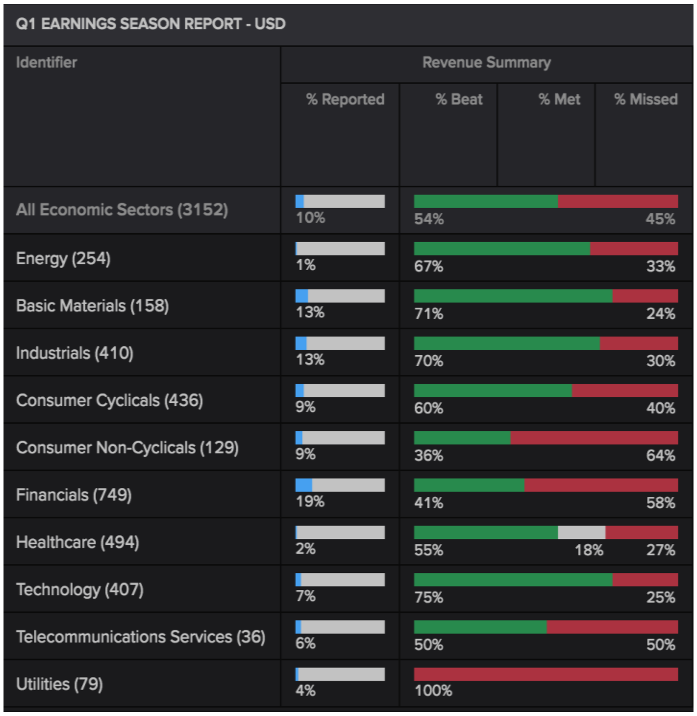


The details of this plan, the big one being whether or not a border adjusted tax (BAT) is included, could help spawn some movement in the currency markets again. We'll have to keep our eyes on that.

There's also the looming threat of a government shutdown on the 29th (this coming Saturday). You can read more about that in this piece from Nordea Markets.

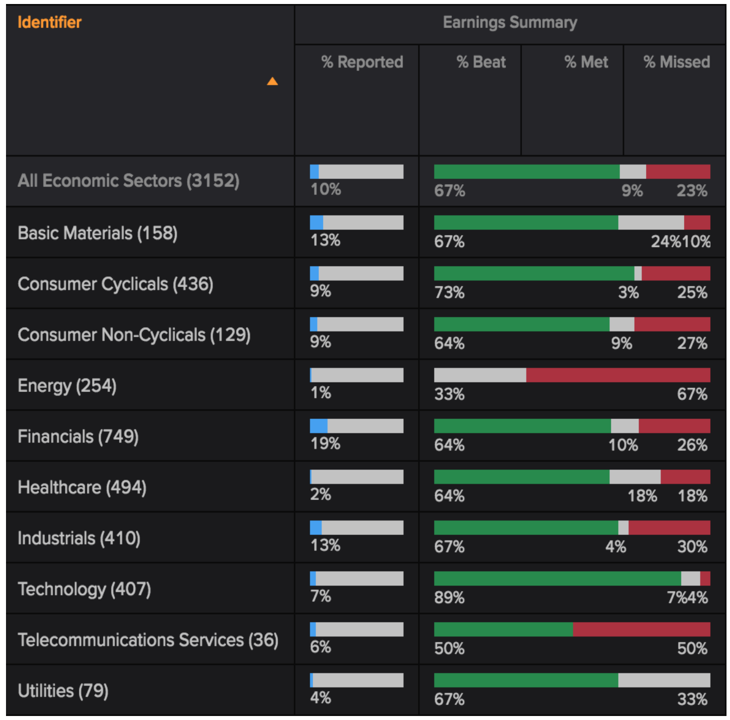
And finally, this is a BIG week for earnings… the biggest earnings week in over a decade actually. More than 190 members of the S&P are releasing their numbers this week. That's over $7.7T in market cap and around 40% of the benchmark's total value. Expectations are high and this quarter is set to mark the strongest growth in quarterly earnings in over five years.

You can see the beats and misses by sector for both revenue (left) and earnings (right) below. So far just 10% of the market has reported. But of that 10%, 67% have beat on earnings and 54% on revenues. Technology continues to be the big winner and consumer non-cyclicals one of the losers.



Q1 EARNINGS SEASON REPORT - USD

Identifier	Revenue Summary % Reported	% Beat	% Met	% Missed
All Economic Sectors (3152)	10%	54%		45%
Energy (254)	1%	67%		33%
Basic Materials (158)	13%	71%		24%
Industrials (410)	13%	70%		30%
Consumer Cyclicals (436)	9%	60%		40%
Consumer Non-Cyclicals (129)	9%	36%		64%
Financials (749)	19%	41%		58%
Healthcare (494)	2%	55%	18%	27%
Technology (407)	7%	75%		25%
Telecommunications Services (36)	6%	50%		50%
Utilities (79)	4%			100%



Identifier	Earnings Summary % Reported	% Beat	% Met	% Missed
All Economic Sectors (3152)	10%	67%	9%	23%
Basic Materials (158)	13%	67%	24%	10%
Consumer Cyclicals (436)	9%	73%	3%	25%
Consumer Non-Cyclicals (129)	9%	64%	9%	27%
Energy (254)	1%		33%	67%
Financials (749)	19%	64%	10%	26%
Healthcare (494)	2%	64%	18%	18%
Industrials (410)	13%	67%	4%	30%
Technology (407)	7%	89%	7%	4%
Telecommunications Services (36)	6%	50%		50%
Utilities (79)	4%	67%	33%	

I think (hope) Republicans will choose *not* to shoot themselves in the foot and make the right choice by avoiding a government shutdown but I have little faith in politicians regardless of political color, so we'll see. Trump's tax proposal *should* wow markets and fuel another leg higher. But I may be asking too much. And earnings should continue to come in strong to mixed, giving little challenge to the bullish narrative. Either way, I think the balance at the moment is in favor of the bulls.

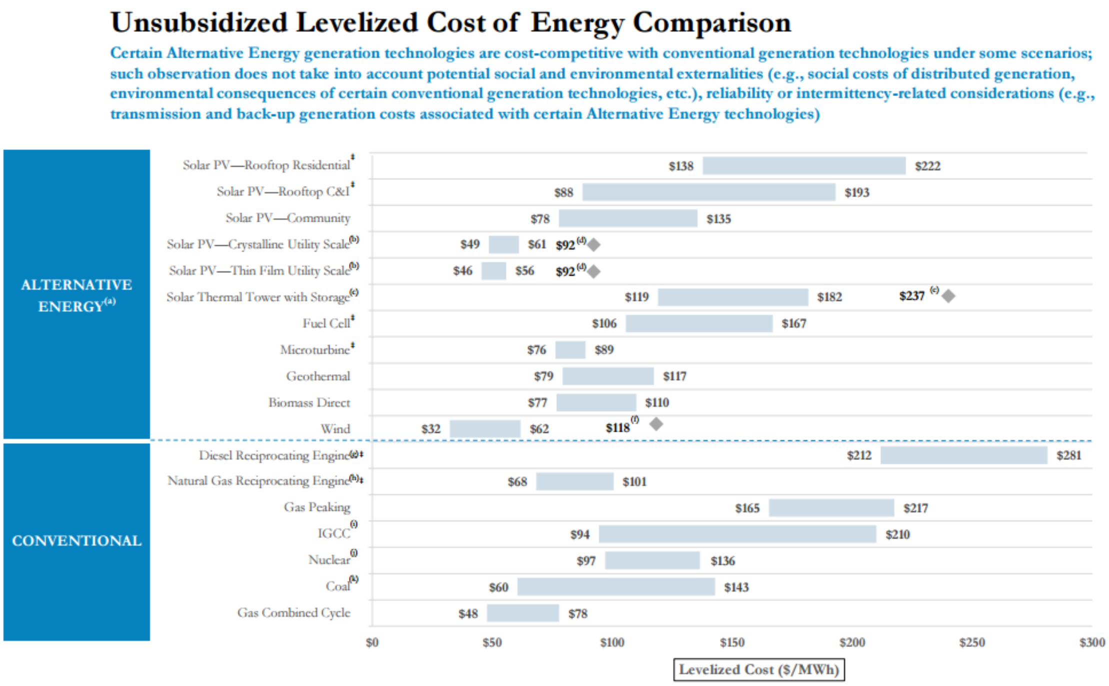
On an unrelated note, the following charts have piqued my interest. The data below describes a long-term secular theme that'll have many second and third order impacts (especially geopolitically). I suspect there'll be plenty of big trades to be made off this theme over the next few years. We'll have to continue to dig and think about it.

Last week, the UK had its first coal-free day since the Industrial Revolution… nearly 140 years ago! You can read the Bloomberg article on that here.

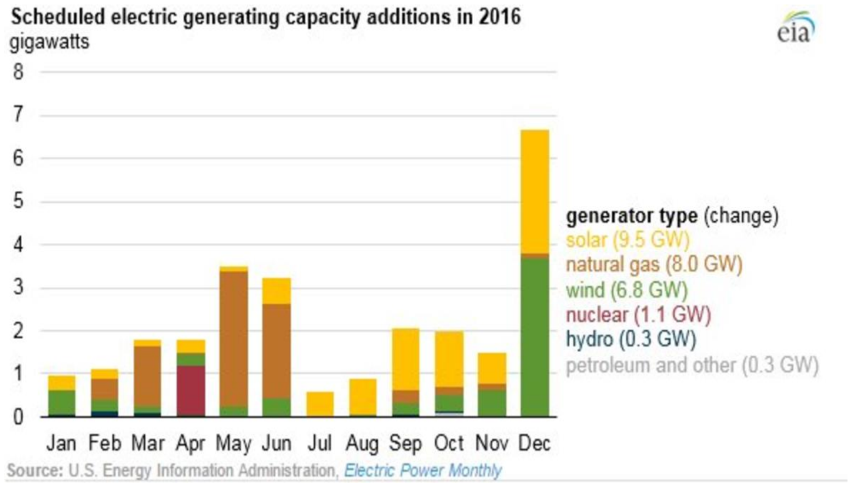
The UK now gets roughly half its electricity from gas, 30% from renewables, and the remaining from nuclear power. The UK government is planning to switch off all coal power plants by 2025. (Remember when the 2020s sounded like the distant future? Now it's just a few years away... I swear time is picking up speed.)

Anyways, just a decade ago the thought of a developed country not using coal as a significant source of its energy was unimaginable.

This energy trend is no longer being driven by wasteful government subsidization but instead by basic economics. Due to technological advancement and scale, wind and solar are now (in many scenarios) competitive with the cheapest forms of carbon based energy. Take a look at the following graph from Lazard:

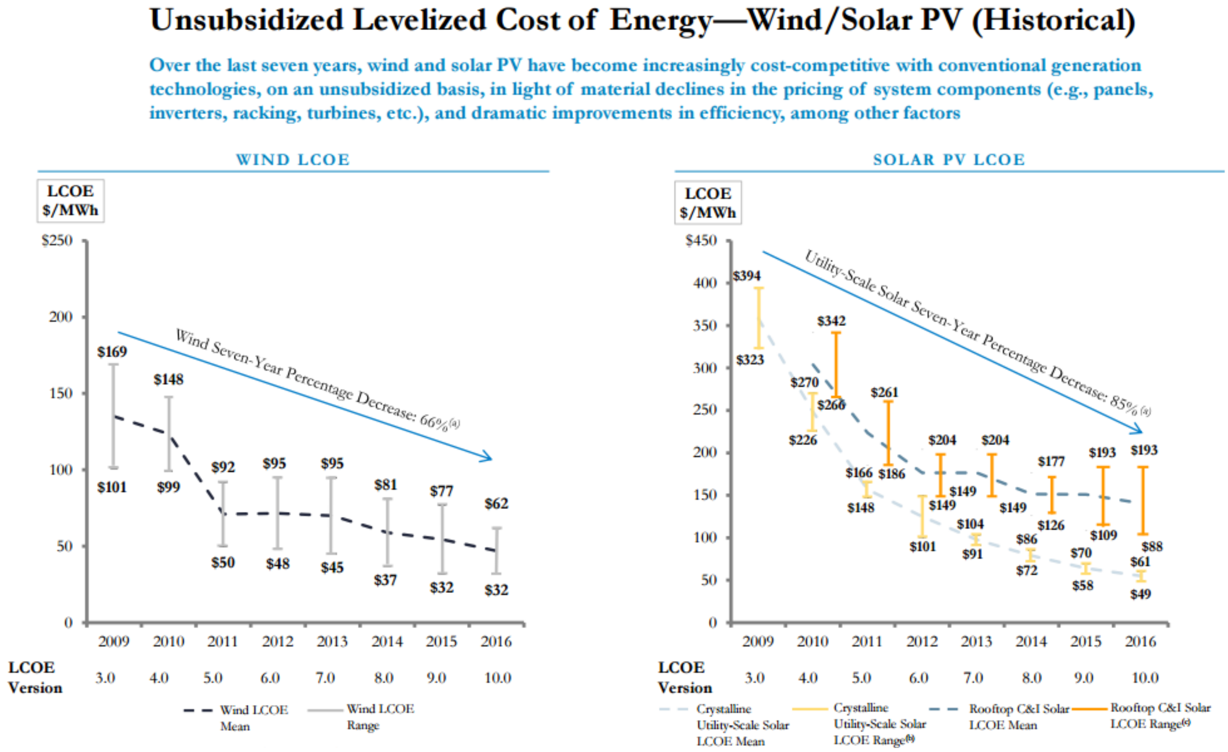


Energy's new economics are leading to more and more alternative energy capacity to come online — a trend you can see in the EIA chart to the right.



Saudi Arabia is planning to build out 10 gigawatts of renewable energy over the next six years. China and India are planning to build so many nuclear reactors over the coming decade that it feels like we'll see one on every corner, just like Starbucks… And China in particular plans on spending close to $400B on wind and solar over the next three years alone. If you've ever travelled to China and choked on their black, coal-filled fog, then you understand the sense of urgency.

This trend is happening all over the world and will only continue as greater scale spurs increased investment. This will bring down costs and lead to even greater adoption. A reflexive competitive pricing advantage is being created in renewables. And that's saying nothing about the social and environmental drivers also behind the trend.



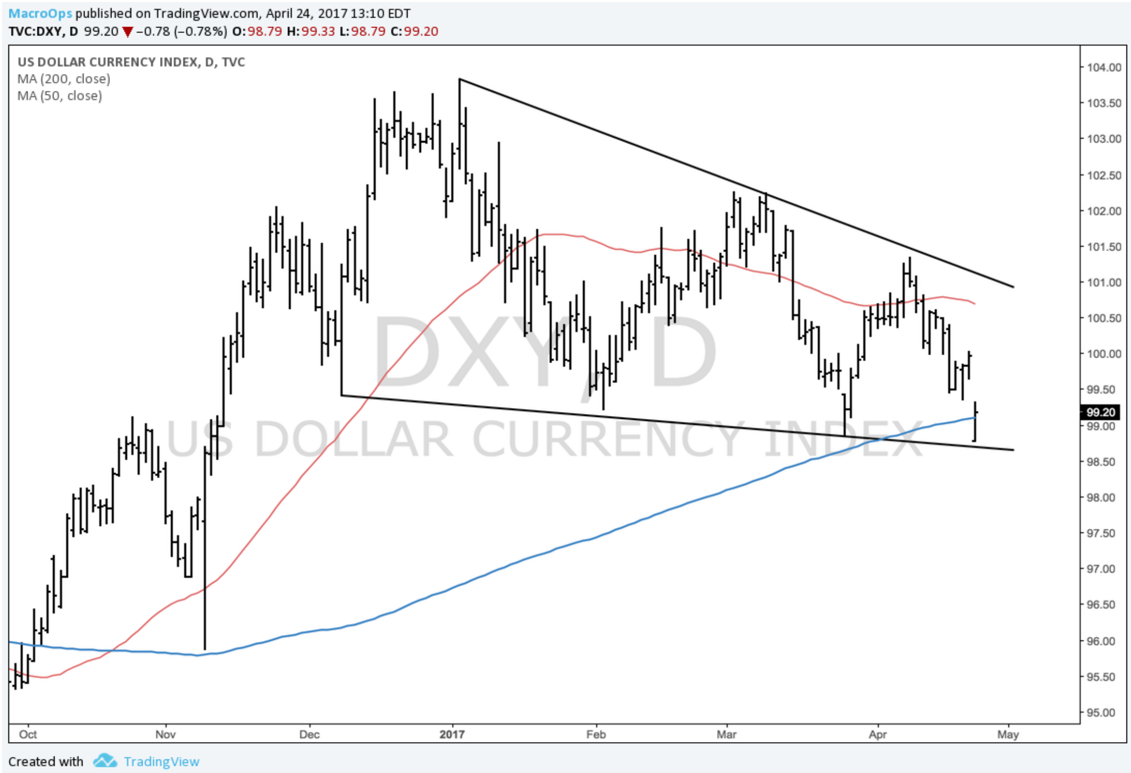
Anyways, this is just something I'm thinking about. It's a long-term trend and the world will still be burning plenty of fossil fuels well into the foreseeable future. But there is a definite tectonic shift going on in the energy space which makes me wonder what kind of impact there'll be on the future pricing of things like oil and coal, if any. You can find the slide deck from Lazard here.

I'm a luddite. I'm interested in technology only if it can help me with my work or if there's a trade to be made off it. Tyler and Anish like to give me crap because I don't know how to snap on the Snapchat (it's a horribly confusing platform, imo). But this video of a real demo of Magic Leap augmented reality both excites and scares me. Watch this right now.

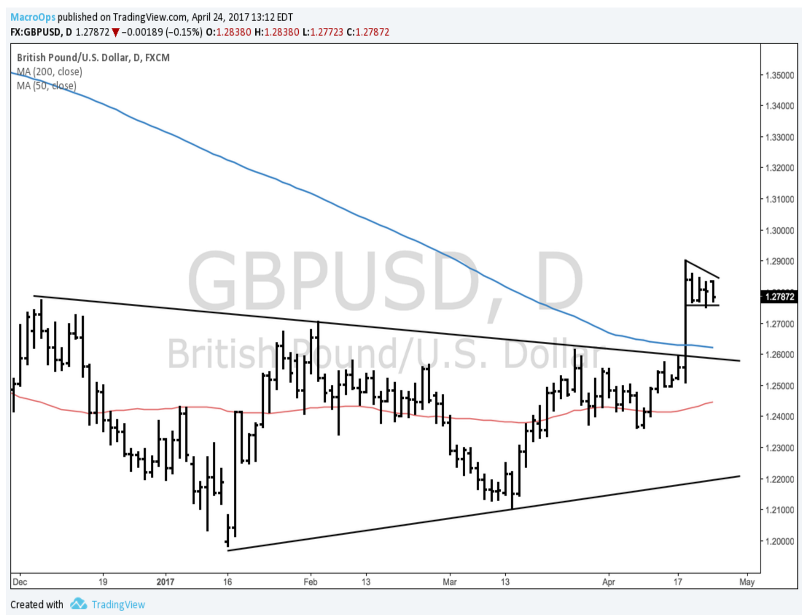
Nuts, right? Benedict Evans of Andreessen Horowitz has a really good write up (here) on where this technology is headed and its potential impacts.

Lastly, here's a video from David McWilliams, one of the very few economists I actually like. It covers the potential for a coming war between the Fed and President Trump. It's short (just a few minutes) and worth a watch. If you, like me, are a fan of good punk rock music I suggest you check out his older youtube series called Punk Economics.

Markets and Potential Trades

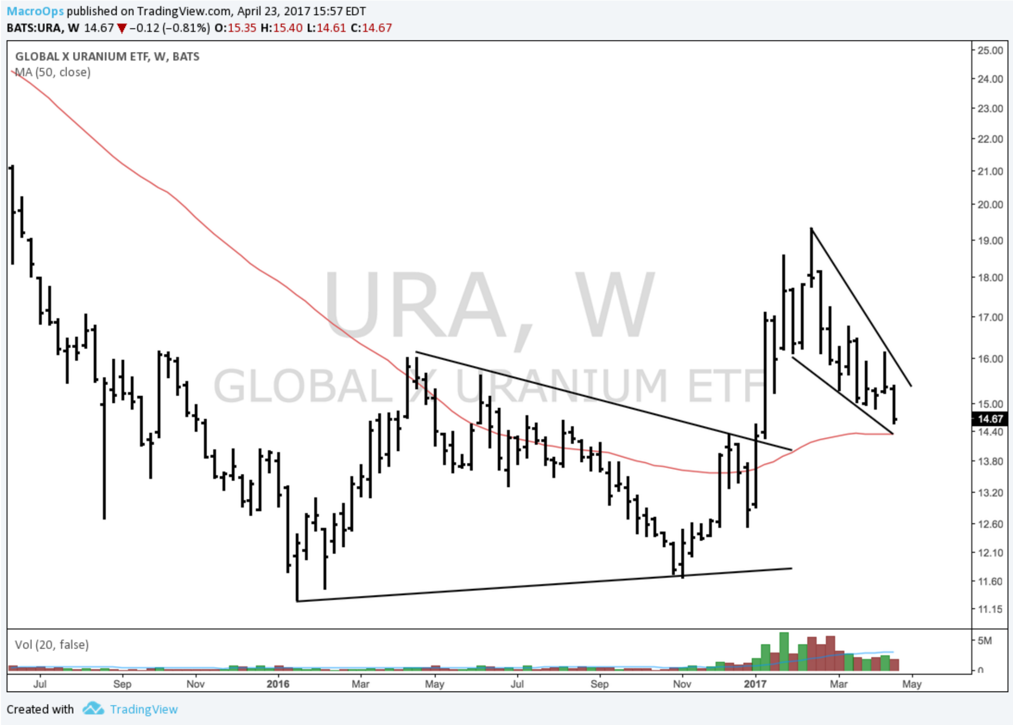


The dollar is down at the bottom of its consolidation pattern. If there's a decisive break below this range we may finally see that long dollar shakeout I've been expecting for a while now. We'll put some short dollar trades on if this happens. My favorite is still the pound which looks like it may be forming a short-term bull flag (chart on your right).

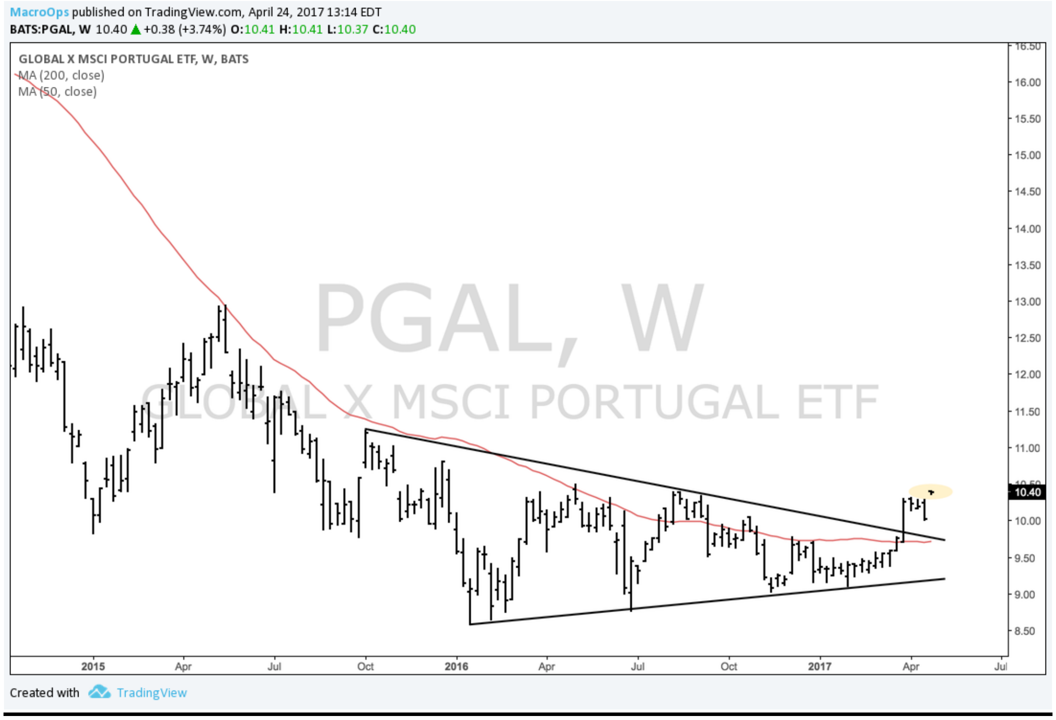


I remain agnostic on oil and gold, but my longer-term bias is that they move lower from here — I'm still cyclically dollar bullish and I think that'll drive both down over the coming year. I don't feel inclined to play either at the moment.

I still like Uranium and will continue to track it. The basing process for commodities tends to take some time. It's early days in the uranium bull story. If we see some constructive price action we'll probably take a shot at establishing a small position with a wide stop.



We missed the initial entry on PGAL — the global MSCI Portugal ETF. It gapped up 350bps on the French election news. I don't like chasing but because of the upside asymmetry to the trade we're going to put on a small starter position on the open tomorrow.



I'm also thinking about going long Deutsche Bank (DB). It looks like it's forming a large inverted H&S bottom. And if Macron is successful, then EU breakup worries should secede until Italy's elections next year. This will alleviate the political risk factor that's been keeping the ECB's foot on the QE gas. I suspect this will strengthen the narrative for expectations of a move by the ECB towards tighter policy. Tighter policy would mean higher rates and that translates into greater net-interest margins (NIMs) for European banks (ie, more profits).

We may put on a position before a completion of the pattern with a stop below the right shoulder.

I'm still digging into Stratasys (SSYS), the maker of commercial 3D printers. It's a mixed bag so far.

They've seen falling sales the last few years and backorders have been declining. The bullish case would be that the declining sales are temporary for this young industry. And there's potential for huge upside should tax reform happen. US companies will repatriate a large portion of the cash they're holding overseas. This would likely lead to a boom in CAPEX, which has been extremely weak these past years. Increased CAPEX would in turn drive top and bottom line growth for SSYS.

I like the price action setup so much I'm tempted to put on a small position before I come to a full conclusion. Invest first, and investigate later as Soros would say.

Ah, and almost forgot. One other company I'm digging into is Sequential Brands Group (SQBG). They're a retail company that owns a number of brands like Martha Stewart, Joe's, Emeril Lagasse, GAIAM, Avia athletic wear and others.

Admittedly, I don't know anything about fashion or brands. And the retail space hasn't been doing too well. But SQBG is down 80% from its 15' highs and trading at just 5x free-cash-flow. They just brought in a new CEO, Karen Murray, who's got an impressive resume and track record in the retail space. And insiders have been buying up the stock these last few months.

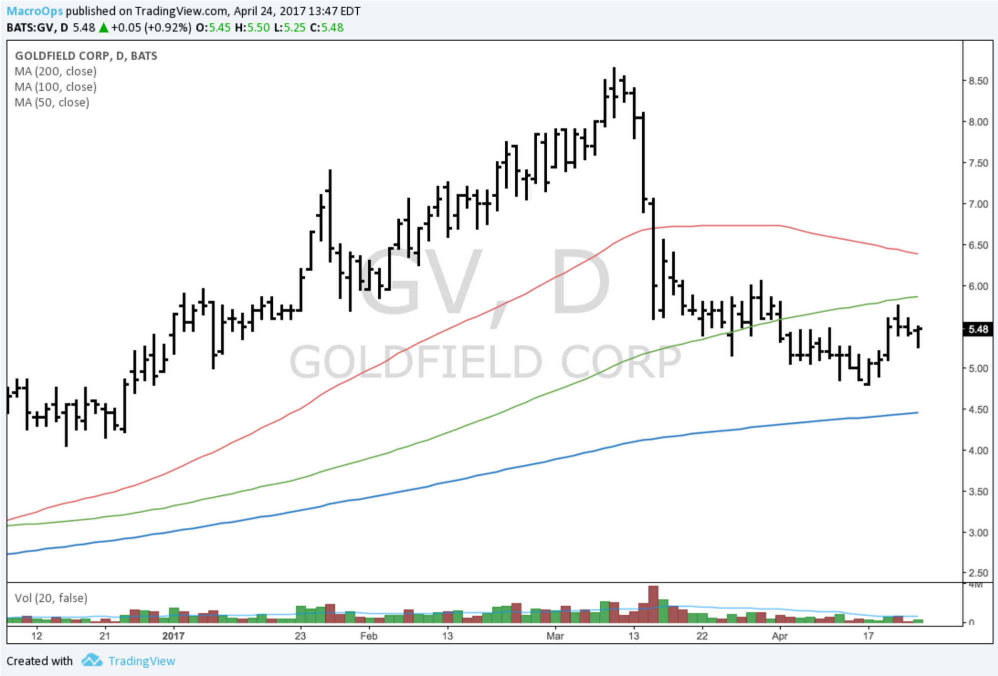
I've still got a lot to look through but there might be a compelling trade here. I'm going to talk with the company this week and see if I can get a better feel for whether a turnaround in the biz is coming.

We'll see. I dig through tons of companies every week and usually just come away uninterested. There's an increasing lack of value in this market. But I figure if I drill a hundred wells where 99 end up being bone dry, I may still get that one that's a gusher and pays for all the hard work on the others.

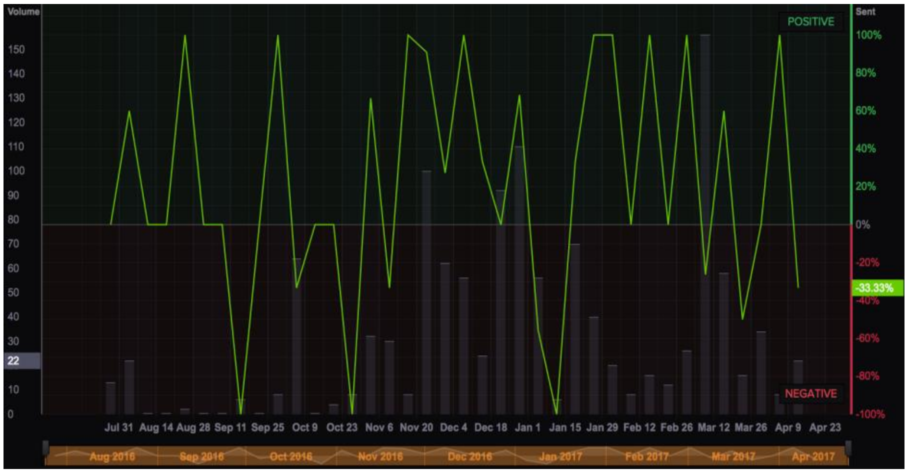
Strat Ops Portfolio Review

Goldfield (GV)
Original Entry Date/Price: **11/15/16 — $3.10**
P&L: **$34,950.10 (includes previous partial exits)**
[Tear Sheets](#)
[Trade Updates](#)

Goldview (GV), which we only have a tiny position in after closing out most of the trade and taking profits, continues to consolidate near its 100-day MA. Its earnings come out May 15th and I still really like the company.



I expect it to consolidate and maybe have another move down, shaking out the remaining weak longs. Sentiment became too bullish on the stock — which tends to happen when a stock doubles in just a few months. Retail sentiment is starting to move back to negative territory (this chart is from our Reuters Eikon sentiment application). I'd like to see it fall further and if the numbers look good when earnings come out in a few weeks then we'll build back our position.

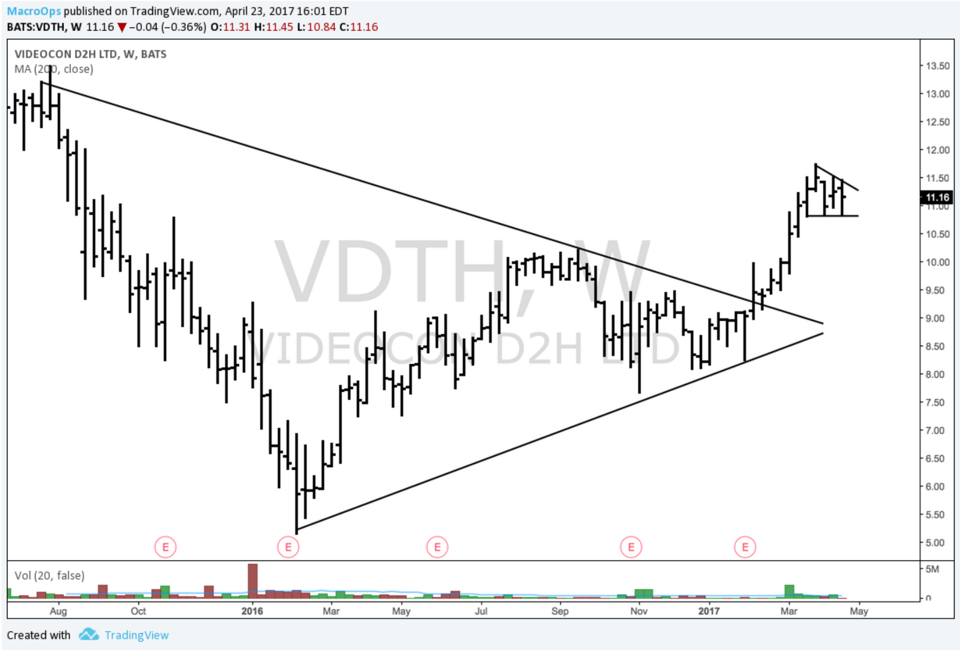


Gaia (GAIA)
Original Entry Date/Price: **3/23/17 — $9.74**
P&L: **$11,165.00**
Tear Sheets
Trade Updates

GAIA continues to move higher. Earnings come out May 8th, so we'll have more to talk about then.

Videocon (VDTH)
Original Entry Date/Price: **3/23/17 — $11.27**
P&L: **($1.139.00)**
Tear Sheets
Trade Updates

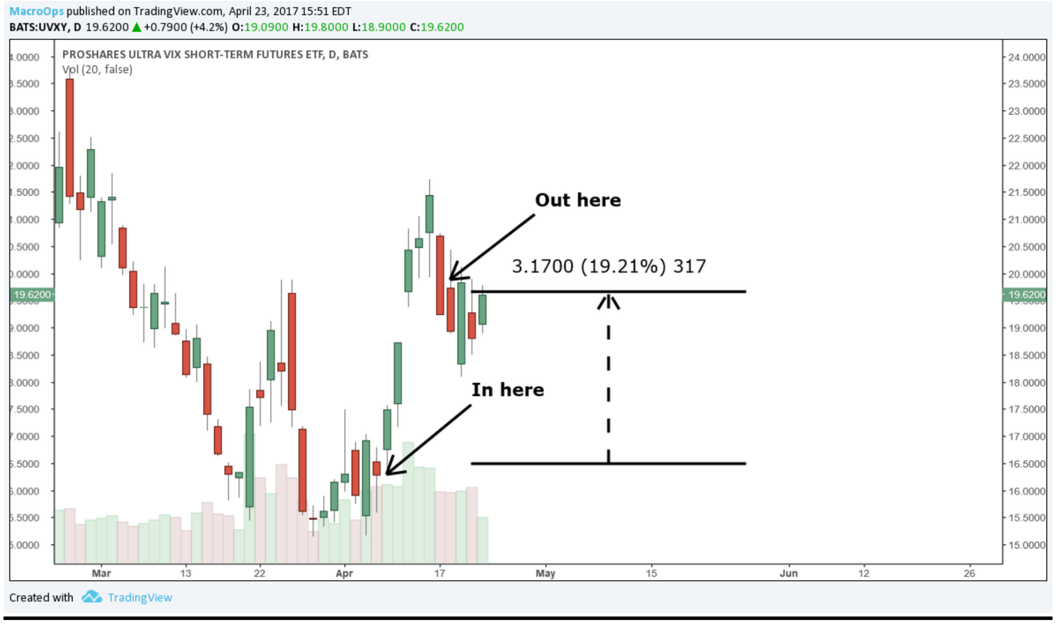
VDTH continues to consolidate. I like the broader action in the Indian market, which is undeniably bullish. The company's earnings release isn't until May 22. If there's a strong breakout to the upside of this range then we may use that as an opportunity to pyramid onto our initial position.



Vol Ops Portfolio Review

<u>UVXY</u>
*Entry Date: **4/6/2017***
*Entry Price: **$16.50***
*Exit Date: **4/17/2017***
*Exit Price: **$19.67***
*P&L: **$23,616.85***
[*Trade Updates*]

We took our pre-election vol trade off last Monday for a nice 19% gain in 11 days.



At the time it was tough to tell whether a premature exit was the right move. The original plan was to wait until Friday. But the volatility term structure had already inverted. This lowered the odds of more follow through.

When UVXY was in the 16s, there was an 80% chance of higher prices. But at the higher Monday price level the probability of prices appreciating even more was no better than a coin flip. We didn't have an edge.

Our Monday exit turned out to be pretty damn good. UVXY continued to trade sideways with a few nasty drawdowns. We didn't give up any upside by exiting early.

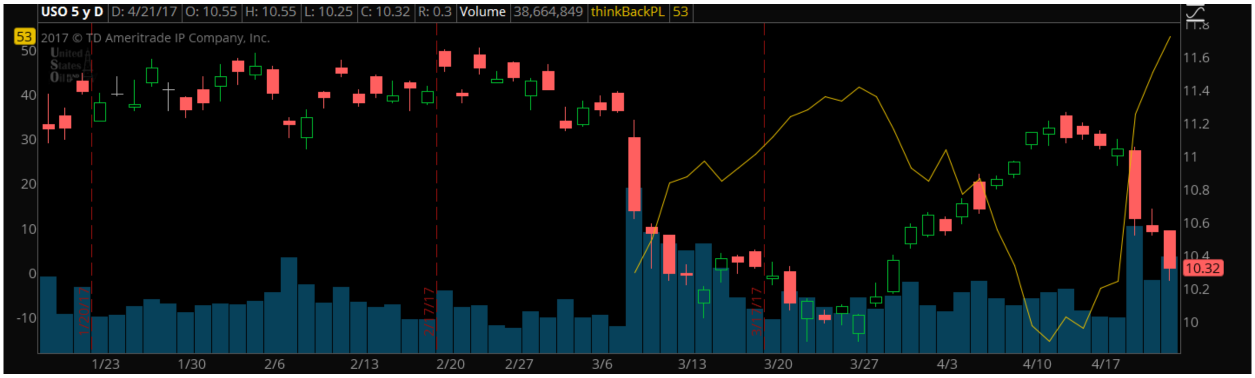
CL 48.5 April Puts
Entry Date: ***3/8/2017***
Entry Price: ***$1.06***
Exit Price: ***$0.00 (Expired worthless)***
P&L: ***($11,155)***

Our busted crude short finally rolled off this week. The out-of-the money put options expired worthless and we took a full loss.

This trade is a great reminder of just how hard it is to go long options over short/mid time horizons. So many things have to go your way to win. The crude puts we bought had cheap vol but it didn't matter. Like we talked about in our latest options article, if you don't delta hedge, buying an option is more of a bet on trend than higher volatility.

Crude moved around a lot since our initial entry but we didn't get a trend. Mean-reversion prevailed.

We would have had a max winner if we sold ATM calls. The chart below shows the price action of USO against the equity curve of a short ATM call in yellow.



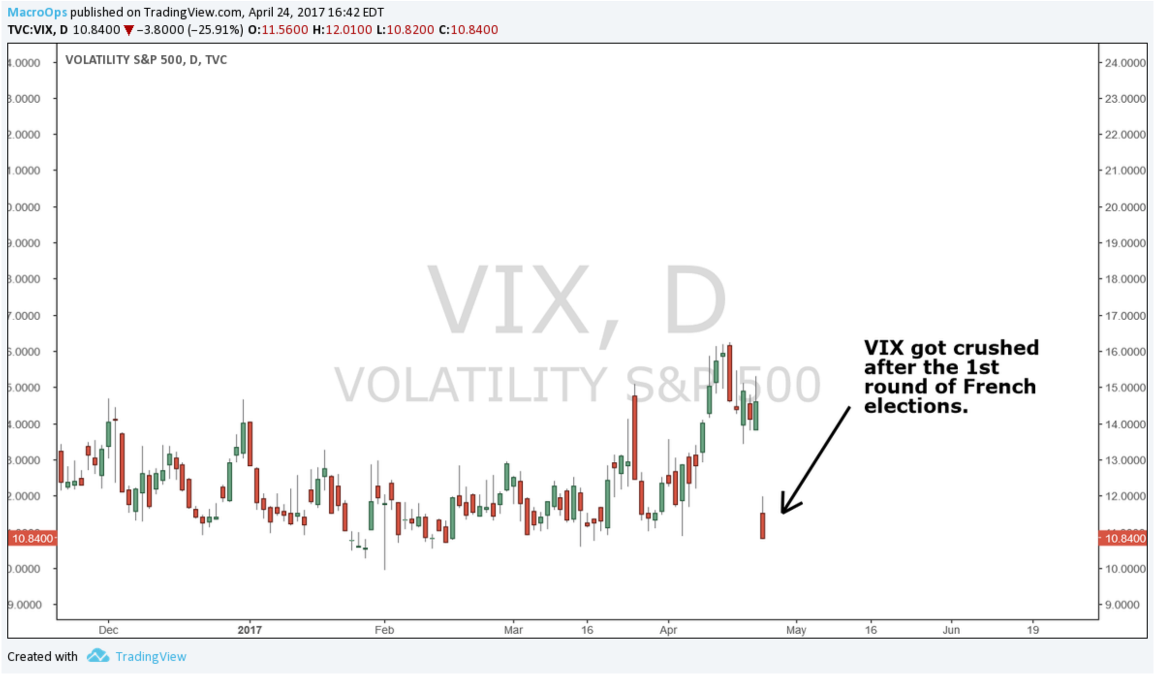
The call started trading for $0.53. The most expensive it ever got was around $0.63. Call sellers barely took any heat on this trade and walked out with max profit. That's a far cry from what happened in our trade.

Once again, using a long option ended up costing us. The lesson here is simple. Avoid buying options unless you have super-high conviction that a trend will complete. Expecting "higher vol" is not enough.

Going forward we'll only use the short side of options to bet on direction if the trade has a time horizon under 90 days. It's foolish to fade the advice of a macro legend like Jim Leitner. (Scroll down to the "options" section if you don't know what we're talking about.)

June VIX Futures/SVXY
Entry Date: ***3/20/2017***
Entry Price: ***$15.00***
P&L: ***$61,470***

Volatility sold off hard after Sunday and we are up huge on our short VIX futures. The VIX had one of its largest one-day down moves in history finishing at -25.91%!



We didn't expect this big of a move after round 1, but hey — can't complain when you're making gobs of money.

FXE (EURUSD) Straddles
*Entry Date: **4/21/2017***
*Entry Price: **$7.20***
*P&L: **($6,682)***
Trade Updates

We just placed this long-term trade last Friday. The idea here is simple. We want the Euro to break out of its extended 2-year range. The direction of the break doesn't matter. We're hoping the French elections will serve as a catalyst.

Fellow Operator, Thomas, came up with an even better way to execute this trade. You can read up on his original idea in the Comm Center here.

He found that the 103/105 strangle had the same breakeven price as FXE, but at 85% of the cost. The one downside is the higher probability of a max loss. With the 104 straddle you only take a max loss if FXE expires exactly at 104. But with the 103/105 strangle you'll take a max loss if FXE expires anywhere between 103 and 105.

If you haven't executed this trade yet, be sure to check out that 103/105 strangle! And if you've already bought the straddles that's fine too. Both should pay out handsomely if we get the range break.

Vol Ops hit a new high last today! As long as vol remains subdued, we expect *Vol Ops* to continue with its outperformance.

And with that I'll bid you adieu. Hit us up on email or in the CC if you've got any questions or come across any compelling trades or interesting info.

P.S. here are two great quotes from Van Tharp I came across. A lot of truth in these...

> *I'm not saying that controlling your mental state is the magic solution to trading success. It's just part of the answer. But when you admit that the answer is within yourself, you've come a long way.*

> *The realization that you are responsible for the results you get is the key to successful investing. Winners know they are responsible for their results; losers think they are not.*

Portfolio Snapshot

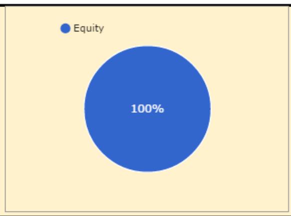
Strategic Ops

NAV $1,166,865

Asset Class	Position	Size	Cost Basis	Risk Point	Open Risk	Target	Notional	Beta
Equity	Goldfield GV	1,000	$3.89	$2.52	$1,370.00	$4.50	$5,250	0.9495
Equity	GAIA	7,600	$9.88	$8.50	$10,488.00	$13.75	$79,040	0.4097
Equity	Videocon VDTH	2,900	$11.27	$9.26	$5,829.00	$17.45	$32,335	0.7855

Metrics

Exposure Breakdown	
Equity	$17,687.00
Commodity	$0.00
Fixed Income	$0.00
Forex	$0.00



Total Open Risk

$17,687.00

1.52%

**Updated 4/24

Volatility Ops

NAV $1,272,518

Asset Class	Position	Size	Cost Basis	Notional
Volatility	June 21st VIX Future	-36	$15.00	-$543,600
Equity	SPX May 18 2390 Call	19	$12.80	~
Forex	FXE Jan 2018 104 Straddle	80	$7.20	~

Scenario Analysis/Stress Tests

Max Loss -$350,000

**Updated on 4/24