MARKET BRIEF Death, Toil, And Ignorance

Charles MacKay wrote in *Extraordinary Popular Delusions and the Madness of Crowds* that, "Three causes especially have excited the discontent of mankind; and, by impelling us to seek remedies for the irremediable, have bewildered us in a maze of madness and error. **These are death, toil, and the ignorance of the future…**"

"Ignorance of the future" drives price action in markets.

This is because, *Ignorance*, or not knowing, spawns fear. And fear is the most powerful human emotion.

Whether it's the fear of capital loss or the fear of missing out… the four letter F-word is deeply ingrained into the mind of the speculator.

The reasons for this are evolutionary. A strong fear response kept certain individuals alive. Those individuals then when on to procreate.

Varying levels of ignorance cause varying levels of fear. The result is various fear responses that equate to various buy and sell decisions.

I believe ignorance and its child "fear" are at the root of all poor human behavior.

A big part of successful trading — and living — is rooting out your own ignorance, or at least learning to live with it, so you don't act (trade) off it.

But I digress…

The chart above shows Bitcoin's near 20,000% rise over the last four years. Price has popped vertically since the start of 2017.

Parabolic moves like this aren't typically healthy. This is FOMO driven price action reminiscent of every other popular bubble (ie, tulips, south sea, tech stocks etc.) throughout history.

To be honest I'm not a bitcoin expert. I've learned enough about it to not care to learn more.

I think the blockchain technology that supports it is interesting. But the "currency" argument for Bitcoin is not.

Its sole value is based on greater fool theory, meaning it's only worth what another is willing to pay. And when you have a digital, ephemeral, non-asset backed "currency" in a parabolic bubble, prices are completely dependent on a growing base of buyers. Eventually, and always, the buyers exhaust themselves. The rug gets pulled out from under the lofty prices and maximum pain is felt by those left holding the bag.

The argument that the US dollar or any other government issued currency is no better is nonsense.

The dollar is backed by the full faith and credit of the US government. This government has sovereign over trillions of dollars worth in resources and the ability to tax some of the most productive and wealth accretive assets in the world. Same too with the Norwegian Krone, Swiss Franc, and on and on.

Bitcoins don't have cash flow. Even gold has a number of actual uses.

I get that perhaps a lot of Bitcoin's recent rise is due to Chinese capital fleeing the country… the cryptocurrency is particularly useful for that. But even that won't go on forever.

That's just my two cents (in $ not Ƀ). I think it's fine trading Bitcoin, I'm just not interested in "owning" it for the long-haul. I admittedly wanted to buy some to trade after favorable price action over a year ago, but alt-currencies aren't covered in the mandate from the people I manage money for. Oh well...

It'll probably go higher from here, at least for a while. But if you're buying without a hard stop at these levels you're crazy.

Either way, the rabid bitcoin crowd could benefit from reading MacKay's work. His wisdom would help Bitcoin diehards regain their senses and see the latest rise for the madness that it is. As Mackay said: "Men, it has been well said, think in herds; it will be seen that they go mad in herds, while they only recover their senses slowly, one by one"

Speaking of currencies, the dollar finally puked out of the lower bound of its wedge. I noted in last week's Brief that this was a move I've been waiting for. If it continues to follow through, and I think it will, then it'll be one of the most important macro drivers over the next 1-3 months — which is about how long I think the move will play out.

The two forces of mean-reversion and trend are constantly pushing and pulling all assets.

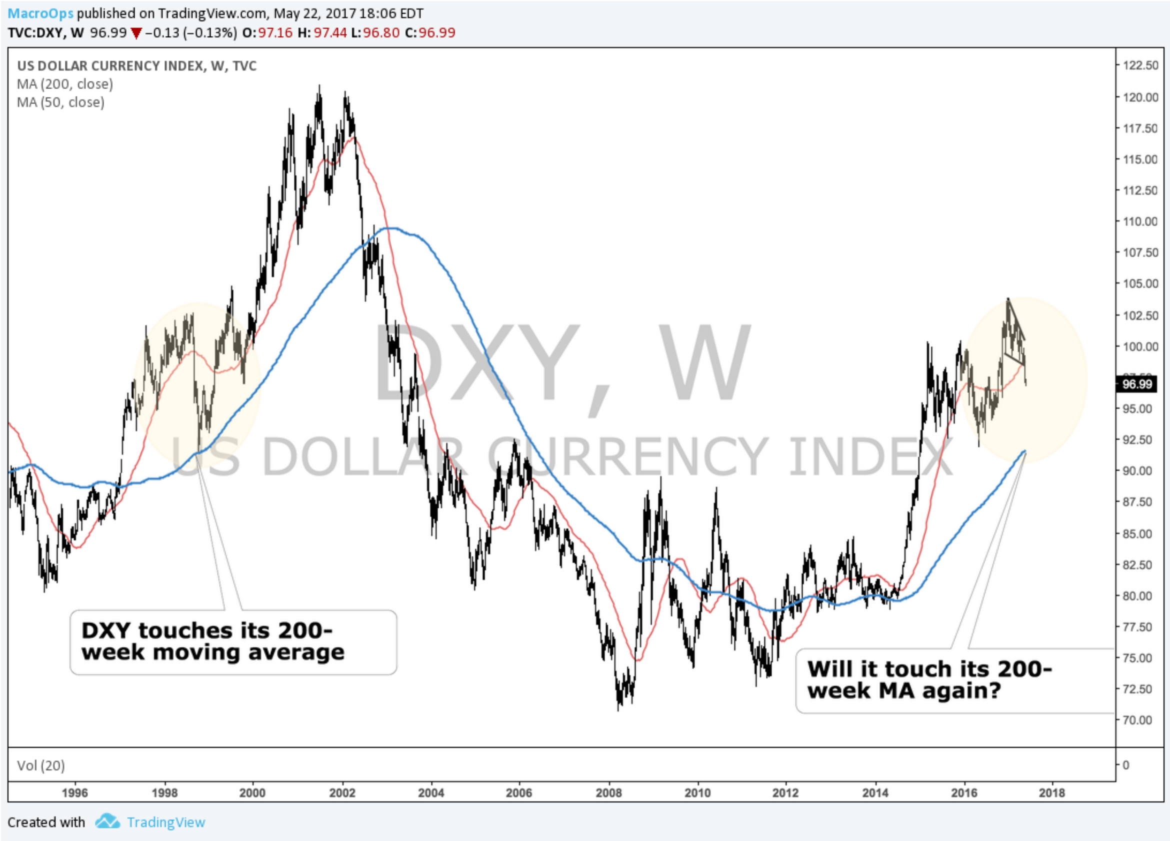
There are logical positioning reasons behind this. The longer an asset trends, the more one-sided positioning becomes. This leads to powerful trends with fewer and fewer retracements. But in the process this creates weak and complacent holders as well as crowdedness. Eventually the tide turns and investors are forced to rush to exit all at once. This leads to large counter-trend retracements where mean-reversion dominates and the weaker hands are shaken out.

We've talked a lot about how the 98'-99' macro analog is a very helpful to understanding today's environment.

Both periods experienced a gun shy Fed that kept rates too low for too long, leading to large asset price inflation. This boosted the US economy relative to the rest-of-the-world and caused speculative capital to flow into the US and create a dollar bull market. The dollar bull market in turn drove commodities lower and eventually led to an emerging market crisis (experienced in 98' and 15').

There's plenty of differences as well (no analog is perfect) but I think the late 90's is a very helpful reference point for the market today.

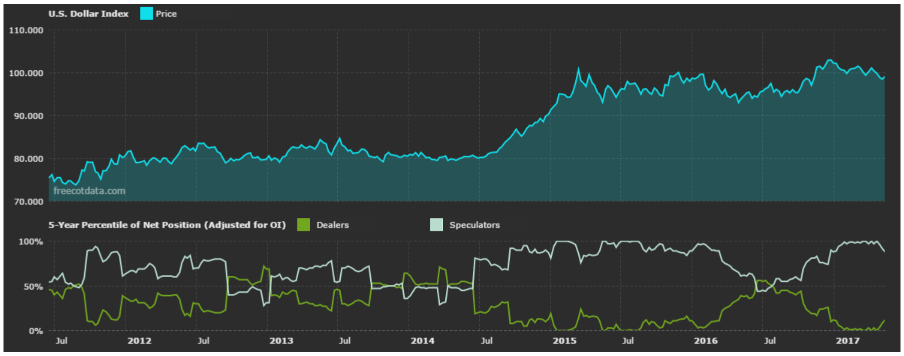
Using this analog and looking at the chart below showing the dollar on a weekly basis over the last 20-years, you can see why I'm cyclically a dollar bull but a bear in the near term.

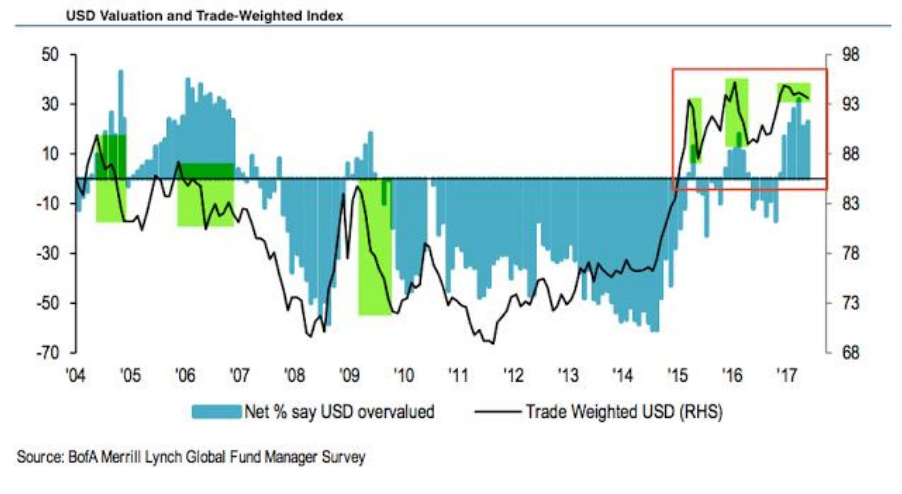


The yellow circle highlights the period in 98' that I think today's dollar will mimic. That would mean a further fall of around 5.5%, down to just below the 92 level to touch its 200-week moving average.

The move would see mean-reversion exerting its temporary control over the broader dollar trend.

The dollar has long been one of the more crowded trades as noted in the COT report (shown right, blue line denotes speculative longs) and the BofA Fund Manager Survey. That means there's a lot of complacent and weak longs sitting in a crowded trade.





Like 98', I think the dollar retrace will be quick and sharp.

As a result of this dollar move I expect US equities to underperform their foreign peers over the coming months. My short-term tactical indicators for the US market are currently reading neutral to slightly bearish. Over the last few months, these showings of weakness have quickly reversed. I'm not so sure that will happen this time but I'll keep you guys posted.

And as we talked about in last week's Brief, a lower dollar will be a boon to precious metals, oil, and emerging markets. There's a lot of potential trades here.

We already have a long GBPUSD trade and long bonds (ZB futures) position which will both benefit from a dollar sell-off. But I think gold looks interesting here for a swing play. Even some energy names look good too.

I'm looking to put on a position in the gold miner IAG this week if the dollar continues to move favorably.

Nautilus, a quant research firm, put out an interesting chart which uses iron ore as a prism to view the tightening/easing cycle by the Chinese government.

China manages its economy with a iron clad grip. And just like its slow and steady devaluation of the yuan, it has managed — at least up until late — to slowly and methodically move from tightening to easing of credit conditions as it attempts to stifle speculation and coordinate a soft-landing for its over-leveraged ponzi economy.

Now I have no doubt in my mind that they'll eventually fail miserably at this. And I chuckle every time I read an economist or financial pundit discuss how China is "different" from other countries that live under normal economic laws. That's ignorance.

If you spend time studying the economic history of Soviet Russia in its heyday, right up until its collapse, you see all the same kinds of talk. Fools suffering from recency bias use extrapolation in place of reasoned analysis to form their opinions.

Anyway, the chart shows how the Chinese government tends to ease following a negative 30% three-month rate of change in the price of iron ore delivered to Qingdao. Iron ore is a useful Chinese bellwether because it's used in their overzealous building and construction.

Nautilus shows prices have recently fallen and hit that 30% pain threshold signalling that the Chinese central planners may loosen the credit reigns for a bit. This would be supportive of global growth, commodities, and emerging markets in general.

forward returns after 5 events 7/13/2009 - 5/18/2017

	MBIO62DA MBUL	MXEF/MXWD	MATR/SPX	FCX (Freeport)	DE (Deere)	PCAR (Paccar)	STLD (Steel Dyn.)	IBOV Index
Event Dates	3Mo	3Mo	3Mo	3Mo	3Mo	3Mo	3Mo	3Mo
07/12/2010	18.88%	4.10%	7.18%	51.09%	31.09%	20.97%	0.76%	12.47%
10/27/2011	13.70%	1.30%	2.23%	7.84%	12.44%	0.66%	20.42%	5.90%
08/29/2012	32.80%	2.51%	2.34%	9.64%	13.09%	10.71%	5.47%	1.45%
04/01/2015	12.32%	-2.11%	-1.44%	-3.00%	9.81%	3.96%	5.46%	0.38%
12/07/2015	48.54%	1.73%	0.80%	26.56%	4.98%	6.53%	22.05%	8.06%
Avg after Signals	25.25%	1.51%	2.22%	18.42%	14.28%	8.56%	10.83%	5.65%
Average All Periods	1.34%	-1.11%	-0.72%	0.77%	3.67%	2.78%	3.94%	1.04%
T-Statistic	3.48	2.54	2.07	1.87	2.39	1.64	1.58	2.07
# Events Up/Down	5 / 0	4 / 1	4 / 1	4 / 1	5 / 0	5 / 0	5 / 0	5 / 0
Significance	99%	97%	95%	94%	97%	92%	91%	95%

Many Chinese stocks, especially tech oriented ones, are going on a run at the moment. I'm annoyed because I was tracking Weibo (WB) and even covered it in a Brief a few weeks ago. It had formed a solid ascending triangle and has favorable fundamentals.

But we missed the breakout and the stock hasn't given another entry point since. It's now up over 40% in the last two weeks. I don't feel compelled to chase and will only enter on another technical setup that provides a good R/R entry.

Another play off the weaker dollar reflation theme is going long shippers.

We've been tracking the shipping sector for some time. It's been stuck in a long bear market due to excess capacity caused by easy financing from low rates. Simply put, the shipping sector has suffered from a glut of ships and tepid global trade.

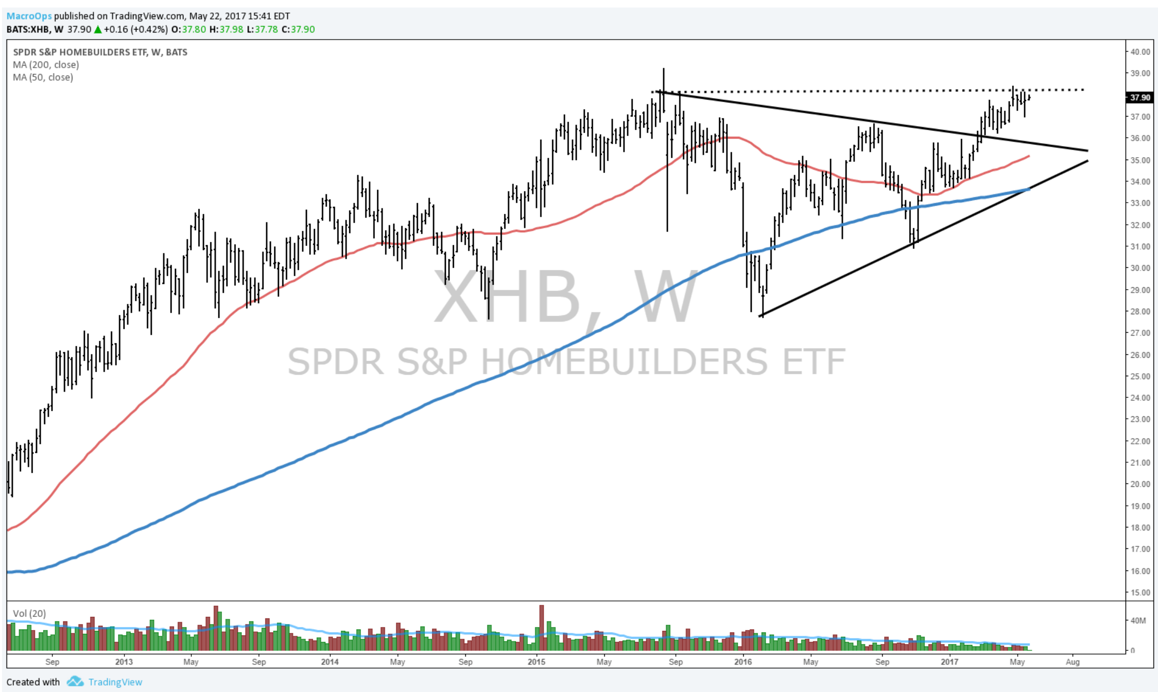
The glut in ships hasn't significantly improved. That won't happen until this credit cycle turns and many of these zombie shippers go belly up with a lot of tonnage getting scrapped. But… for a swing play with a couple of months time-frame, shippers might be lining up for a nice long that'll benefit from Chinese easing and a weaker dollar.

Dorian LTD. (LPG), shown with weekly bars in the chart to the right, is my preferred method for playing a potential shipping revival.

LPG is a stock we covered in the past and owned for a short-time last year. It's one of the best run shippers and operates in the niche space of moving liquefied petroleum gas. The stock has formed a nice 15-month cup with handle base. Its price has been trading in a tighter and tighter range over the last two months. It looks like a coiled spring. We'll put on a long position on a strong move to the upside.

Another space I'm watching are home builders. Millennials are beginning to buy their first homes and this trend will pick up as the labor market continues to tighten and nominal wage growth picks up. Like the shipping sector, though not to the same extent, the real estate market suffers from an overhanging supply glut left from the previous housing bubble.

With that said, the price action and narrative concerning the housing sector look constructive. We'll continue to dig and release research if we find any compelling stocks in that space.

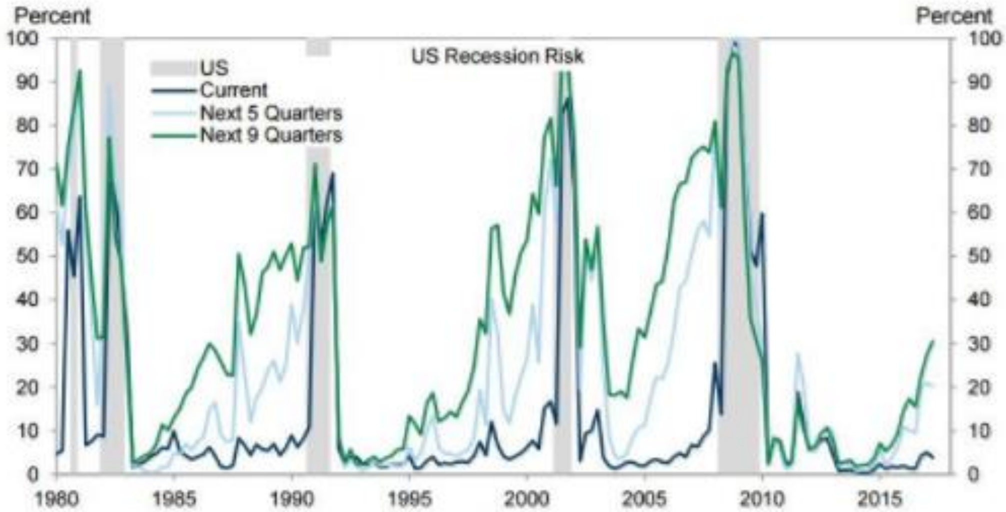


Other than that, we're still closely tracking the uranium and the soft commodity market. Potash producer IPI is close to triggering a buy signal. We'll put on a starter position if wheat looks like it's about to get going (potash follows the price action in soft commodities like wheat where it's used as a fertilizer).

There's a lot of political noise right now. Though a lot of it's interesting in a political context, I'd largely ignore it from a trader's standpoint. The media will surely interpret and attach these political events to market moves. And though political news will sometimes have very short-term impacts on markets, in the long-term it's just noise. Prices will go where they're going to go in accordance to unfolding economic fundamentals and embedded expectations.

Goldman Sachs recently released their recession indicator which has a strong predictive track record. It shows the cycle is aging but still has room to run — we're in the bottom of the 6th of a 9 inning game. This is inline with the recession indicators we track as well.

Exhibit 1: Recession Probability Rises from Low Levels



Source: Goldman Sachs Global Investment Research

I got back late this weekend from my reunion in Colorado. It was a good time. Though admittedly, by the fourth day we were all ready to go home. A bunch of 30 and 40 year olds can only act like young and dumb 20-something marines for so long until the illusion begins to fade (ie, an old liver can only take so much drink).

I'm still in recovery mode and will be working overtime this week to get spun back on markets and dig into some trades.

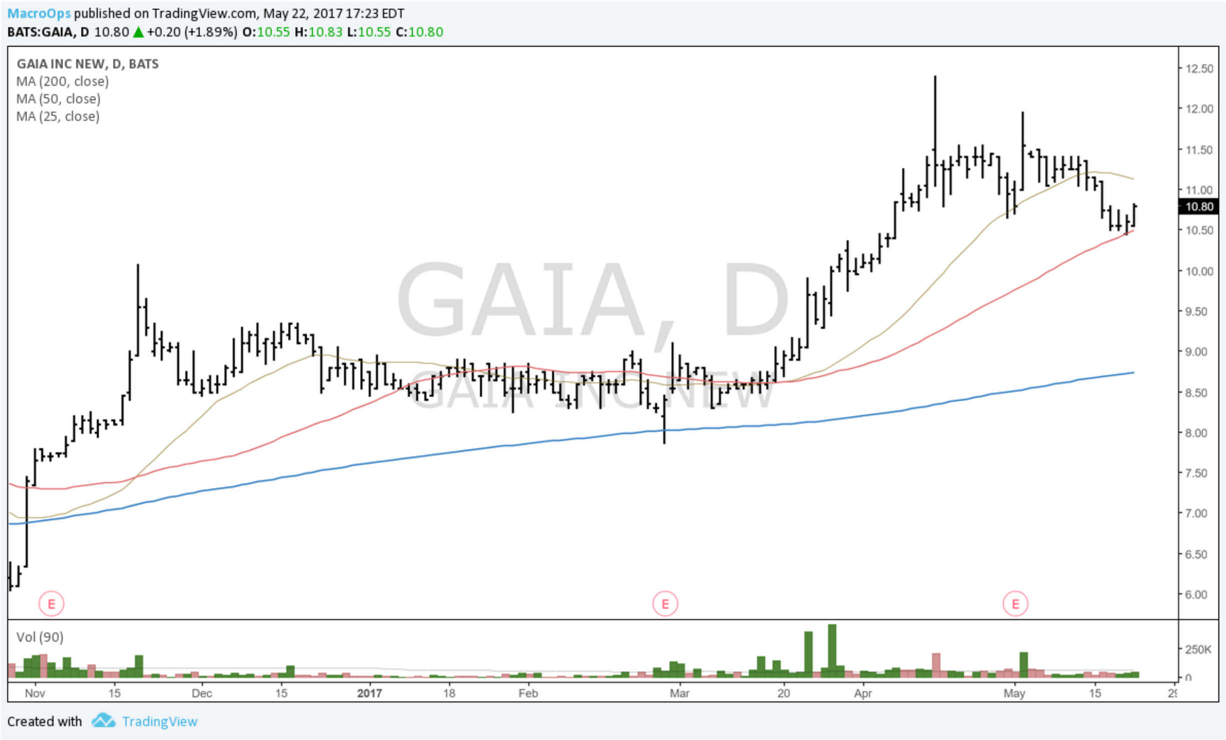
I'll shoot ya'll the research on any potential plays we come across and I'll see ya in the CC where I have a lot of catching up to do.

Strat Portfolio Update

Goldfield (GV)
Entry Date: ***11/15/16***
Entry Price: **$3.10**
P&L: ***($434)***
Tear Sheets
Trade Updates

No news. Still tracking and would like to see a larger shakeout on high volume followed by a quick rebound in price before we build a position.

<u>Gaia (GAIA)</u>
Entry Date: ***3/23/17***
Entry Price: ***$9.74***
P&L: ***$6,972***
[Tear Sheets]
[Trade Updates]



GAIA continues to move nicely. Price has come down and bounced off its 50-day moving average which should act as support from here. This continues to be a long-term hold.

Videocon (VDTH)
*Entry Date: **3/23/17***
*Entry Price: **$11.27***
*P&L: **($713)***
Tear Sheets
Trade Updates

The merger between VDTH and DishTV India remains on-track and VDTH continues to be undervalued. The company has earnings next week. We should hopefully get an update on merger progress along with a favourable reaction in the stock's price.

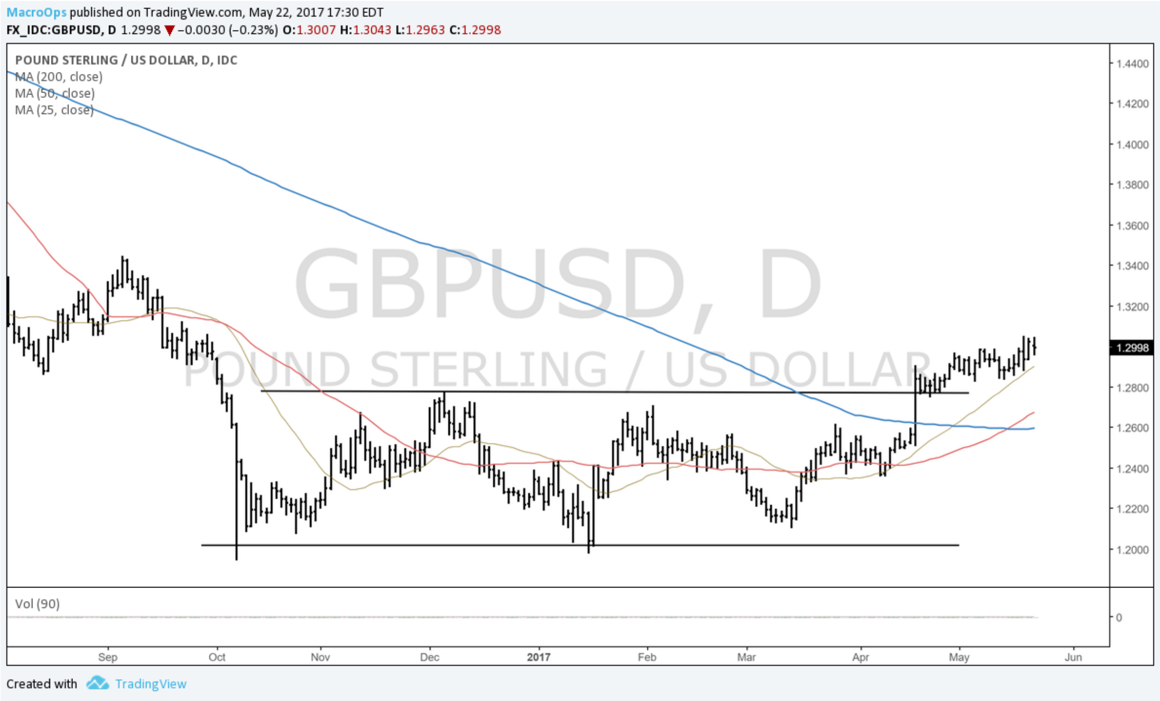
Portugal ETF (PGAL)
Original Entry Date: ***4/25/17***
Entry Price: **$10.57**
P&L: ***$5,423***
Trade Updates

PGAL is strong. The european recovery narrative is picking up steam and this ETF looks like it's at the beginning of a much larger move.

Stratasys (SSYS)
Entry Date: ***4/25/17***
Entry Price: ***$24.45***
P&L: ***$6,504***
Trade Updates

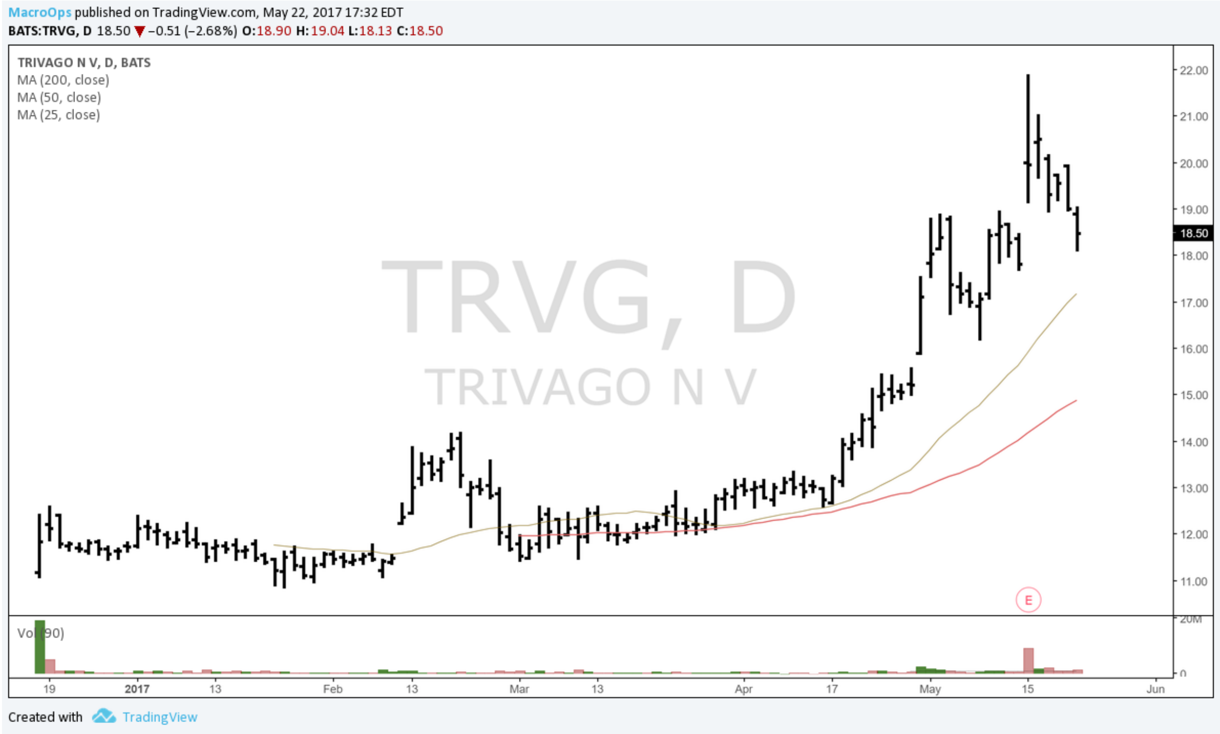
I'm getting bullish on the 3D printer space and price-action on SSYS remains very constructive. I'll look to add to this position on available price action setups.

Pound Futures (GBPM7)
*Entry Date: **4/25/17***
*Entry Price: **$1.2865***
*P&L: **$9,740***
Trade Updates



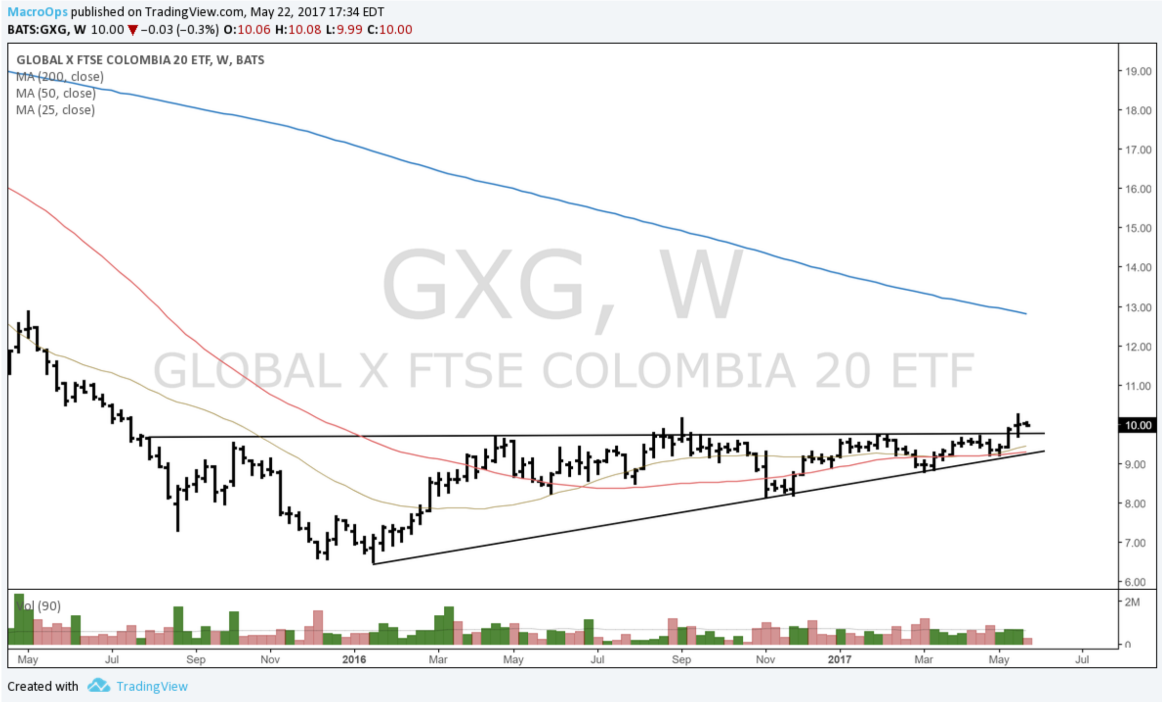
No new updates. Still like the trade and pound should move considerably higher on dollar weakness.

Trivago (TRVG)
Entry Date: ***5/15/2017***
Entry Price: ***$21.16***
P&L: ***($4,668)***
Tear Sheets
Trade Updates



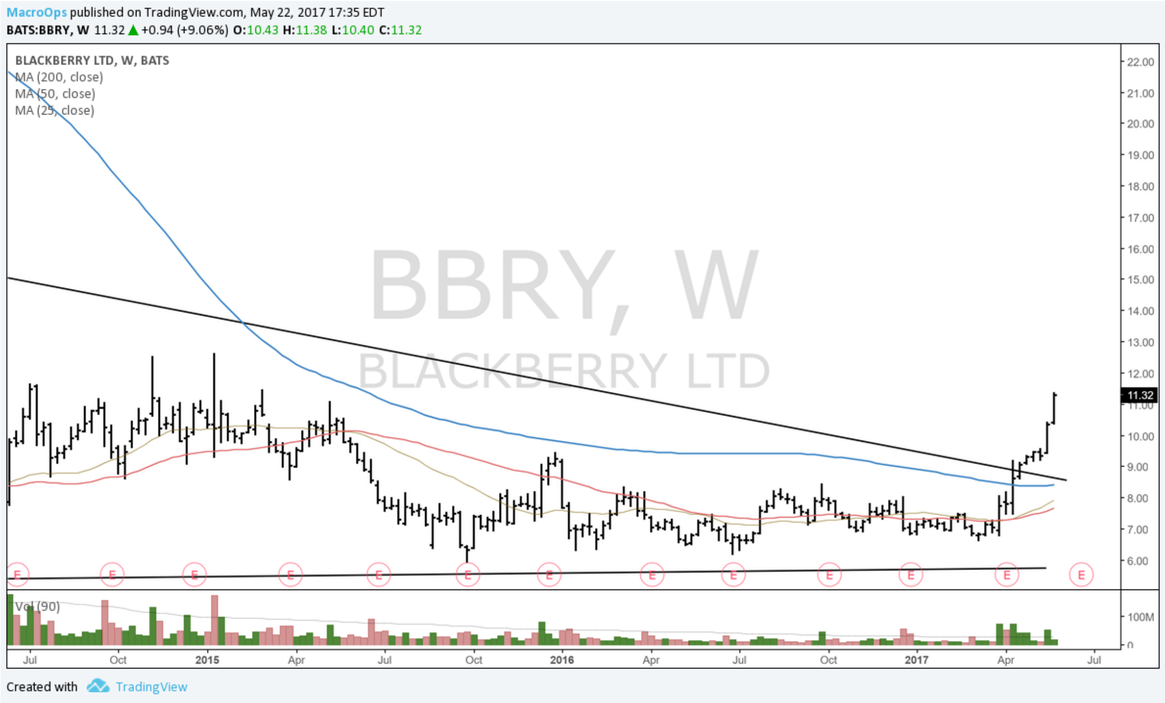
We're down a little on this trade and may get stopped out if price closes below the $17.70 mark. I fear our stop may have been too tight, but such is trading. If we get stopped out, we'll take a tiny loss and move on with the option of taking another swing on a more favourable setup.

Colombia ETF (GXG)
Entry Date: ***5/15/2017***
Entry Price: ***$10.18***
P&L: ***($1,795)***
Tear Sheets
Trade Updates



We should see a strong move in GXG on dollar weakness. I'd like to see a move higher on stronger volume.

BlackBerry (BBRY)
Entry Date: ***5/15/2017***
Entry Price: ***$9.70***
P&L: ***$4,225***
Trade Updates

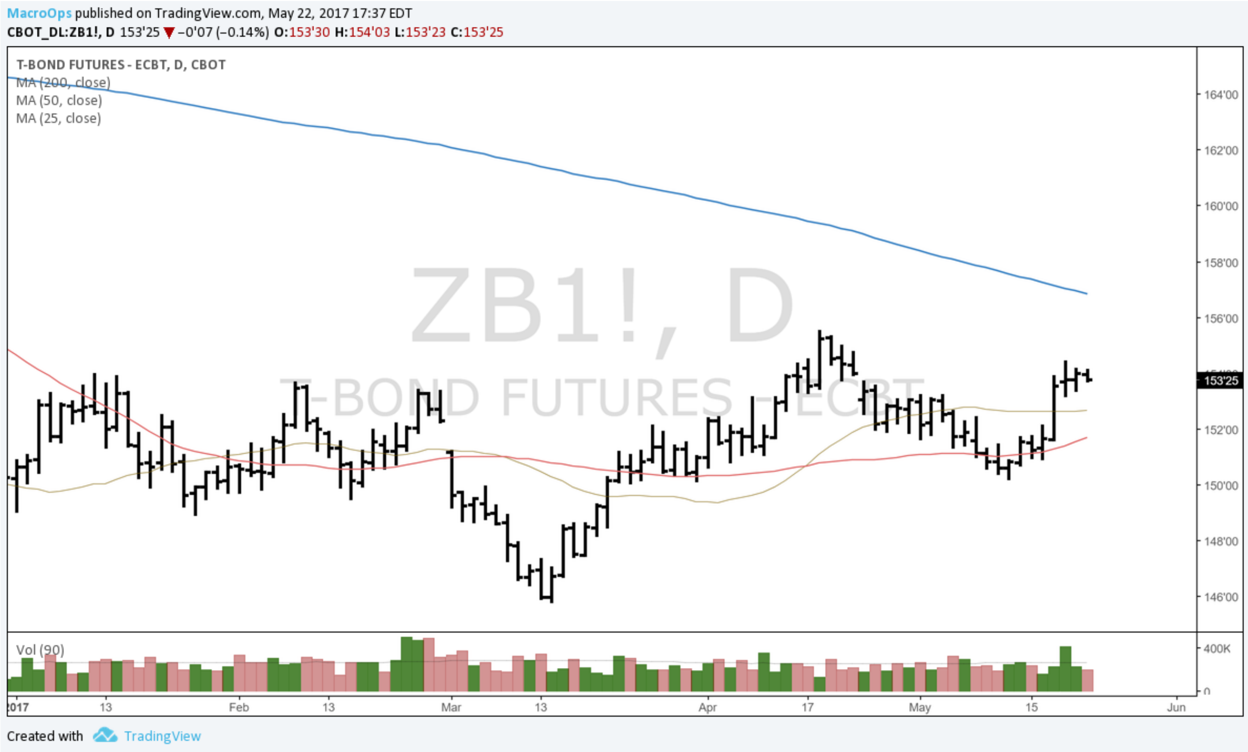


BBRY is now up around 16% since our entry last week. Our position is small because we entered due to strong technicals before we fully got to dive into the fundamental case. If the fundamental picture backs up the price action, we'll look to pyramid onto this position at appropriate R/R entry spots.

<u>Hudson Tech (HDSN)</u>
*Entry Date: **5/15/2017***
*Entry Price: **$8.09***
*P&L: **$777***
[Trade Updates]

Nothing new to report here. This is a great company and the price action is solid. HDSN has much higher to go.

30Yr Bond Futures (ZBM7)
Entry Date: ***5/17/2017***
Entry Price: ***$153.81***
P&L: ***($355)***
Trade Updates



We'll have to roll these next week should we decided to continue holding. That decision is dependent on how the market internals look; whether they've improved or not. We'll keep everybody posted as the week unfolds.

Vol Portfolio Update

August VIX Futures/SVXY
Entry Date: ***5/18/2017***
Entry Price: ***$14.72***
P&L: ***$29,233***
Trade Updates

Last week we rolled over and rebalanced our short vol exposure in the vol book.

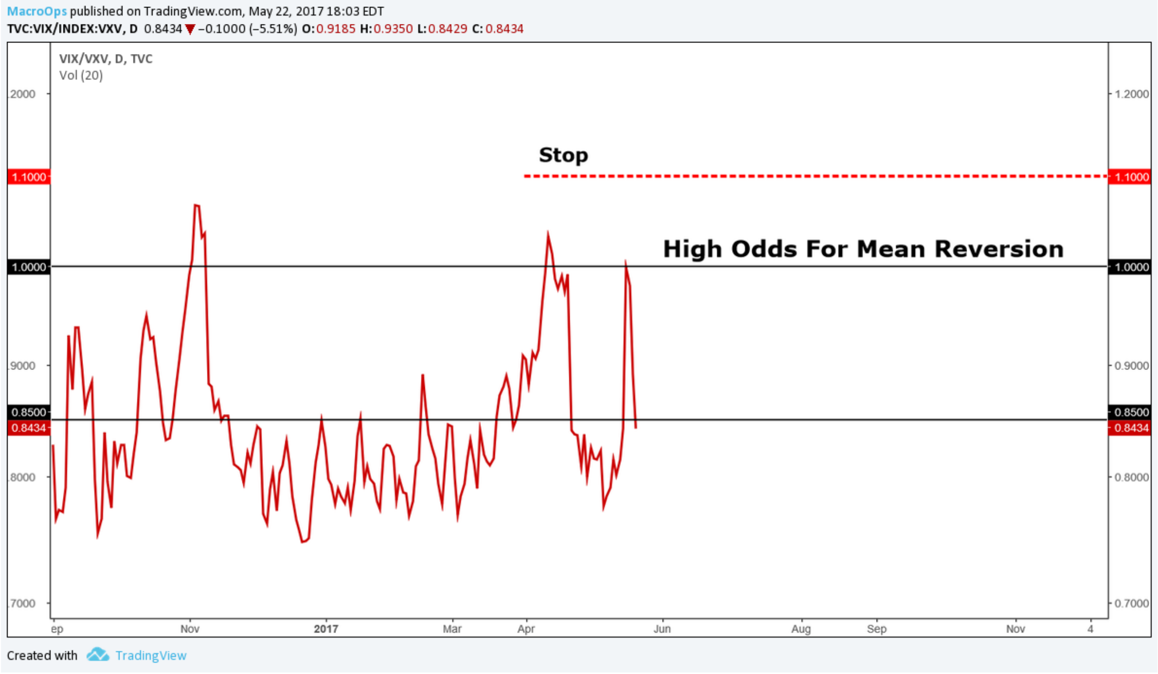
Right as we were about to rollover the VIX had a one-day super spike on Trump impeachment rumors. We figured the move would be short lived since it was catalyzed off of a political rumor and has nothing to do with the underlying macro fundamentals.

But ole' SPX still beat our expectations on how long bad weather would last. Within a day's time the vol event was basically over and VIX is now trading back under 11.

The roll ended up going well. In a mere three days of trading the August cycle is already up 300 bps for us.

For a hot minute we thought that instead of rolling to short August we would have to take a stop on June futures and actually start nibbling on the long side.

But once again the VIX screeched to a halt once the term structure flattened out.



Grain Spread - Short Nov Soy Long Dec Corn
Entry Date: ***5/8/2017***
Entry Price: ***$186.75***
P&L: ***$3,733***
Trade Updates

Last week's Brazil madness was actually a positive event for our grain spread which has now broken out of it's symmetrical triangle to new lows.

Brazil's harvest is just finishing up, so there are plenty of soybeans available for sale there. On May 18th, in reaction to political scandal rumors, the Brazilian Real dropped like a rock,

This overnight currency deval made Brazilian beans more competitive on the global marketplace. To maintain competitive prices the U.S. bean futures had to sell off which is why we got a nice down move on our spread.

<u>FXE (EURUSD) Straddles</u>
*Entry Date: **4/21/2017***
*Entry Price: **$7.20***
*P&L: **($149)***
[Trade Updates]

The Euro is finally holding a trend which means these straddles can start to pay us! The next area of resistance is at $112.00.

We'll evaluate the trade once FXE reaches that point. Until then we need to sit tight and exercise patience.

Portfolio Snapshot

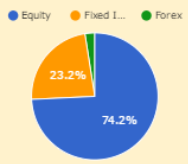
Strategic Ops

NAV $1,169,739

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	1.0694
Equity	GAIA	7,600	$9.88	$8.50	$10,488.00	$13.75	$79,040	0.4497
Equity	Videocon VDTH	2,900	$11.27	$9.26	$5,829.00	$17.45	$32,335	0.7855
Equity	Portugal ETF PGAL	8,000	$10.57	$9.98	$4,720.00	$11.75	$85,040	1.0467
Equity	BlackBerry BBRY	2,600	$9.70	$7.50	$5,720.00	$18.00	$25,038	1.084
Equity	Colombia GXG	10,350	$10.17	$9.62	$5,692.50	$12.75	$105,104	0.6661
Equity	Hudson Tech HDSN	5,300	$8.08	$6.98	$5,830.00	$11.50	$43,142	0.8107
Equity	Trivago TRVG	1,750	$21.16	$17.70	$6,055.00	$30.00	$35,245	-4.961
Equity	SSYS	1,546	$24.45	$21.44	$4,653.46	$31.50	$40,528	1.4414
Forex	Pound Futures (GBPM7)	13	$1.2865	$1.2844	$1,706.25	$1.3300	$1,050,127	0.3216
Fixed Income	30 Yr Bond Futures	7	$153.81	$151.56	$15,767.50	$161.62	$1,076,995	-0.582

Metrics

Exposure Breakdown	
Equity	$50,357.96
Commodity	$0.00
Fixed Income	$15,767.50
Forex	$1,706.25



Total Open Risk

$67,831.71

5.80%

**Updated 5/22

Volatility Ops

NAV $1,310,003

Asset Class	Position	Size	Cost Basis	Notional
Volatility	Aug 16th VIX Future	-38	$14.71	-$530,100
Forex	FXE Jan 2018 104 Straddle	80	$7.20	~
Commodity	Nov Soybean	-5	$959.20	-$240,045
Commodity	Dec Corn	10	$386.30	$194,499

Scenario Analysis/Stress Tests

Max Loss -$350,000

**Updated 5/22