Outside Zebras

Trading Wisdom

> *Zebras have the same problems as institutional portfolio managers like myself. First, both have quite specific, often difficult-to-obtain goals. For portfolio managers, above-average performance; for zebras, fresh grass. Second, both dislike risk. Portfolio managers can get fired; zebras can get eaten by lions. Third, both move in herds. They look alike and stick close together.*
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> *If you are a zebra, and live in a herd, the key decision you have to make is where to stand in relation to the rest of the herd. When you think that conditions are safe, the outside of the herd is best; for there the grass is fresh, while those in the middle see only grass that is half-eaten or trampled down.*
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> *The aggressive zebras, on the outside of the herd, eat much better. On the other hand - or hoof - there comes a time when lions approach. The Outside zebras end up as lion lunch. The skinny zebras in the middle of the herd may eat less well but they are alive.*
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> *A portfolio manager for an institution such as a bank trust department, insurance company or mutual fund cannot afford to be an Outside Zebra. For him, the optimal strategy is simple: stay in the center of the herd at all times. As long he continues to buy the popular stocks, he cannot be faulted.*
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> *On the other hand, he cannot afford to try for large gains or unfamiliar stocks that would leave him open to criticism if the idea failed. Needless to say, the Inside Zebra philosophy doesn't appeal to me as a long-term investor.* ~ Ralph Wanger's "A Zebra in Lion Country"

Ray Dalio says, "You can't make money agreeing with the consensus view, which is already embedded in the price. Yet whenever you're betting against the consensus, there's a significant probability you're going to be wrong, so you have to be humble."

At MO we're outside zebras. We're not inhibited by things like career risk or concerns about what others think about our portfolio holdings. We go after the fresh grass and often stray far from the herd.

But as Wanger and Dalio point out, this can be risky. That risk comes in the greater likelihood of being wrong. So we utilize risk and trade management to account for this higher risk and eliminate the chance of getting gored by lions.

We stay humble and approach every trade with the expectations that it'll be a loser. This keeps us in the proper mindset to manage the downside.

Being an Outside Zebra isn't easy, but it's the only way to get fat.

Markets and Macro

Let's first take a minute and admire Micron's (MU) chart. MU had a beautiful setup that checked every box of the Marcus trifecta; strong fundamentals, great technicals, and was deeply misvalued and misunderstood.

It also held up firm during the market's February selloff. When you see action like that it means the stock is being held by strong hands which is always a positive sign.

MU is now up nearly 30% since our entry a few weeks ago. And our DOTM calls are up somewhere north of 300%. The price of these calls will fluctuate a lot over the coming months. But we have a lot of time left on these. Around 9 months till expiry. So this trade has the potential to be a bottom liner for the year. I just wish we would have bought more. But that's always the case.

Analyst are tripping over themselves to revise their targets for MU higher. Nomura and some others now have it at $100, which I certainly think is possible.

And if MU trades at $100 by November the payout on these calls will be around 14x. Here's the potential P/L graph.

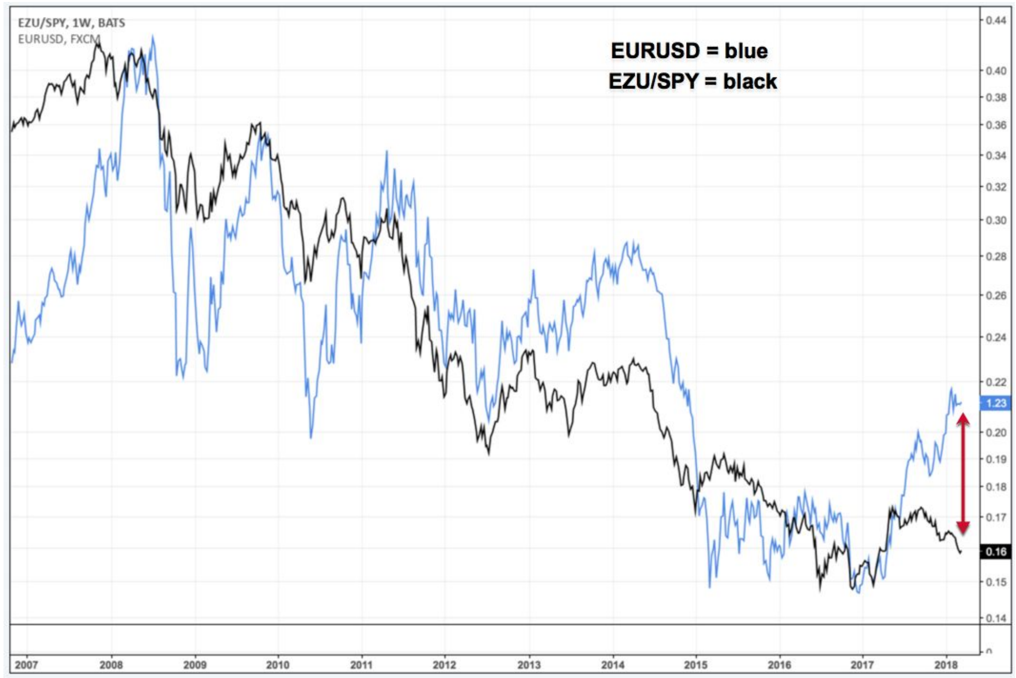
The trade has a budding tailwind in the return of major outperformance by US tech. XLK, the tech sector ETF, just broke out of an ascending triangle. You don't fade this type of price action.

And tech's relative momentum versus the market (XLK/SPY) is accelerating. Relative momentum trends like this often feed on themselves which can lead to a steeper ascent and greater trend persistence.

One of the most important charts right now, in my opinion, is this one. It's the US (SPY) versus the rest of the world (IOO etf) and shows that relative momentum shifted back in favor of US stocks at the beginning of the year.

Relative momentum is important to track because it tells you where large global capital flows are going. And these macro currents are what drive long-term trends and sector/market/asset outperformance.

Speculative flows are also the largest driver of action in the currency market. See the chart below showing European equities versus the US along with EURUSD.



It’s very possible that we’re entering a market ‘melt-up’ period that will be similar in size and speed to that of the late 90s tech bubble. And perhaps this new regime will be led by the US which will put a bid under the dollar. And a stronger dollar will help mute inflation which will prolong the cycle and drive equities even higher, creating a reflexive loop that will continue until a turning point is finally reached.

George Soros explained how this process works in his book *Alchemy of Finance*, writing:

> *To the extent that exchange rates are dominated by speculative capital transfers, they are purely reflexive: expectations relate to expectations and the prevailing bias can validate itself almost indefinitely… Reflexive processes tend to follow a certain pattern. In the early stages, the trend has to be self-reinforcing, otherwise the process aborts. As the trend extends, it becomes increasingly vulnerable because the fundamentals such as trade and interest payments move against the trend, in accordance with the precepts of classical analysis, and the trend becomes increasingly dependent on the prevailing bias. Eventually a turning point is reached and, in a full-fledged sequence, a self-reinforcing process starts operating in the opposite direction.*

If this scenario plays out, then our DOTM strategy should perform extremely well since that's about as perfect of an environment for buying calls that one could ask for. So we're going to continue to dig around and look for names to add to our DOTM book.

We'll also be putting on a position tomorrow in the mattress maker, Purple Innovations (PRPL), that we talked about in the latest MIR. The chart is setting up nicely on this stock and it looks ready to run. The trade has a lot of positive asymmetry to it.

I'll shoot out the trade alert to y'all when we execute.

I've also updated some of the risk points on our current trades. You can find these in the portfolio graphic below.

That's all I've got for this week. Hope you had a good weekend and I'll see you in the CC!

- Alex

Macro Ops Portfolio			YTD	Inception (16')			
NAV	$2,778,002		3.00%	38.28%			

Big Bet Macro

Asset Class	Position	Size	Cost Basis	Risk Point	Open Risk	Target	Last Price
Equity	Limbach LMB	2,750	$13.66	$11.00	$2,475.00	$18.00	$11.90
Equity	JD	5,867	$44.74	$36.00	$56,968.57	$72.00	$45.71
Equity	Interactive Brokers IBKR	1,800	$41.71	$64.60	$16,488.00	$55.50	$73.76
Equity	W&T Offshore WTI	16,000	$2.18	$3.30	$6,400.00	$4.50	$3.70
Equity	Yatra Online YTRA	39,286	$7.40	$6.45	$20,821.58	$14.00	$6.98
Equity	United Insurance UIHC	13,000	$16.98	$18.00	$25,740.00	$20.00	$19.98
Equity	Trip Advisor TRIP	7,754	$36.46	$35.50	$58,387.62	$50.00	$43.03
Equity	MU Jan '19 70 Call	118	$2.12	$0.00	$51,448.00	$10.50	$4.36
Equity	BCS Jan '19 15 Call	574	$0.35	$0.00	$20,090.00	$3.50	$0.35
Equity	DB Jan '19 30 Call	670	$0.30	$0.00	$7,370.00	$3.00	$0.11
Equity	CCJ Jan '19 17 Call	236	$0.41	$0.00	$3,540.00	$5.00	$0.15
Equity	FCAU Jan '19 25 Call	108	$0.90	$0.00	$19,116.00	$5.00	$1.77
Equity	JD Jan '19 70 Call	108	$0.92	$0.00	$11,016.00	$7.00	$1.02
Equity	TRIP Jan '19 75 Call	108	$0.89	$0.00	$7,020.00	$7.00	$0.65
Equity	CHK Jan'19 10 Call	750	$0.14	$0.00	$2,250.00	$1.00	$0.03
Equity	Tesla Mar '18 240 Put	28	$8.80	$0.00	$168.00	$24.00	$0.06
Equity	MS June '18 65 Call	126	$0.46	$0.00	$7,056.00	$3.00	$0.56
Equity	WMT June '18 120 Call	126	$0.51	$0.00	$1,008.00	$3.00	$0.08
Forex	6BH8 Pound Futures	-3	$1.3751	$1.4197	$8,362.50	$1.2457	$1.3852
Forex	6EH8 Euro Futures	-2	$1.2199	$1.2575	$9,400.00	$1.0972	$1.2320

Volatility

Asset Class	Position	Size	Cost Basis	Risk Point	Open Risk	Target	Last Price
Rates	ZNM8 US Note Futures	15	$120.36	Hedge	Hedge	Hedge	$120.03
Rates	IEF March 2018 104/109 St	150	$1.31	$0.00	$31,050.00	$7.00	$2.07
Commodity	SLV June 2018 17 Straddle	130	$2.84	$0.00	$22,880.00	$5.00	$1.76
Commodity	GLD Sep 2018 128 Straddle	24	$15.10	$0.00	$20,640.00	$30.00	$8.60

Risk Budget

	Total Allowed (In Bps)	Total Used	Total Available	Percentage Used
Master	2500	1,475	1025	58.99%
Big Bet Macro	1750	1142	608	65.28%
Volatility	750	268	482	35.79%

**Updated 3/12