A MARKET NOTE

BY ALEX BARROW 5/3/2020

Digestion Mode

Think of the market as a giant collective consciousness with all the trappings and failings of our human ones.

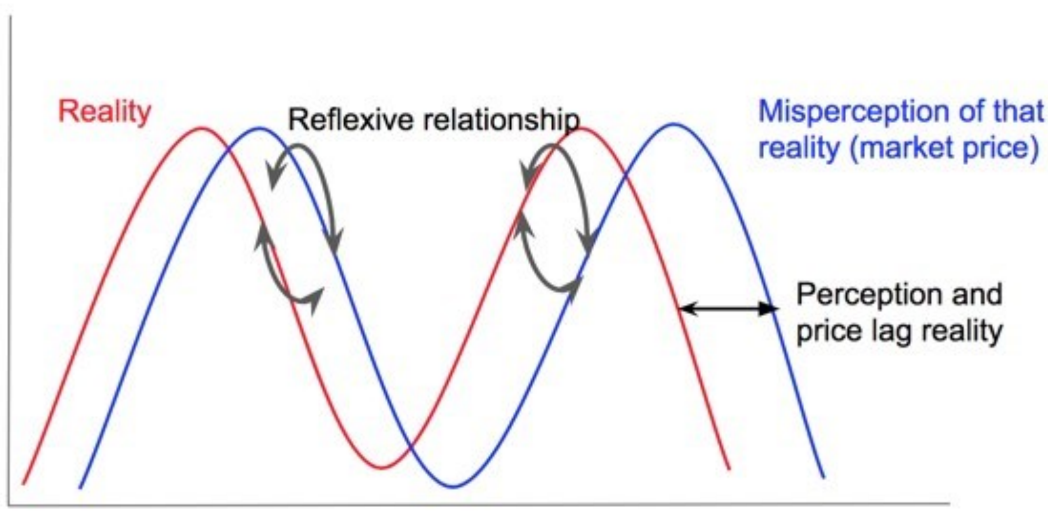
Back in February, this collective consciousness became very optimistic about its future. It was so bulled up that leverage hit records and it decided that paying for insurance against a disaster was a waste of good money — as I noted here in this piece at the time.

This full-blown optimism clouded its judgment. Gave it blinders and biased it against properly discounting some very important changes that had been taking place (ie, the beginnings of a global pandemic with untold consequences.)

But strong sentiment and the associated money flows have a momentum of their own which can create a self-fulfilling feedback loop over finite periods of time. This is what was happening heading into late February. Newton's first law reigned, higher prices beget higher prices, and bullishness beget greater bullishness as the collective consciousness that is the market became careless.

The market was correcting for its mistake in 2019 when it was too fatalistic in its outlook. It had started to price in a recession while the global economy had clearly troughed and was quietly recovering. Not to be made a fool of twice, the market began to over-correct for this error and stopped looking for recession risks… or really any kind of risk at all.

While the market headed one way (up). Reality headed the other (down). And a large narrative/reality gap developed.



All large narrative/reality gaps eventually end and usually do so with the speed and subtlety of a frying pan to the face. As the Palindrome Soros pointed out years ago, they "cannot go on forever because eventually, market prices would become so far removed from reality that market participants would have to recognize them as unrealistic. When that tipping point is reached, the process becomes self-reinforcing in the opposite direction."

Once the reality of the spreading global pandemic could no longer be dismissed, the market reacted as all conscious entities do when confronted with a reality that looks nothing like the one it previously inhabited: it panicked hard and fast.

The panic drove it to reduce its risks (sell-off) at one of its fastest rates in history. The market went from expecting the start of a renewed bull market to seeing the whites of the GFC's eyes in the span of a few weeks.

It saw bank failures, counter-party risks, and liquidity squeezes and acted accordingly. At the same time, policy-makers around the world were thinking the same and started bazooka'ing money into every liquidity provider's pockets, effectively stuffing the financial system with cash in order to prevent a repeat of 08'.

The speed and size of the fiscal and policy responses have been unparalleled. Tough to wrap one's heads around just as is the severity of the economic damage stemming from the pandemic itself.

So the market once again corrected the overcorrection of its original mispricing.

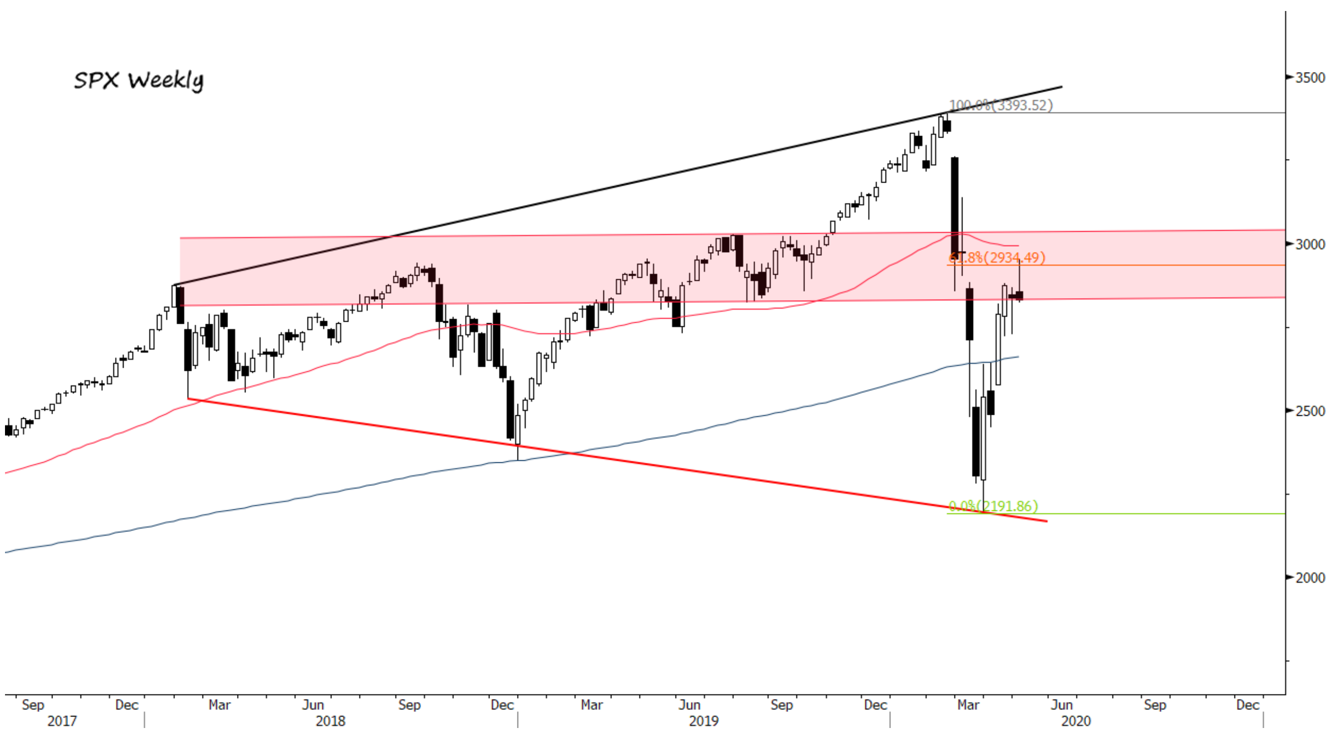
It's now in **digestion mode**. The future is still incredibly murky and multi-path dependent. Our experts don't agree with other experts. The one thing that's apparent is that we're ill-suited to grok and tackle the challenge ahead.

As a result, reality is being squeezed with 20%+ unemployment looking likely in most places amid rolling lockdowns on the one hand and gobbles of money printing and fiscal spending and TINA driven by ZIRP on the other.

Which hand is stronger is anyone's guess. This future doesn't exist quite yet and the market is likely to flail around and grasp at straws until it finds a new plausible narrative to which it can latch onto.

The market is like a stunned fighter after just taking one on the chin from Tyson. It's discombobulated, can't see straight, and wobbly on the feet.

Expect it to act accordingly.



EURUSD broke out of its month-long coil to the upside last week. This could be the breakout that leads to a new trend, or not. EURUSD has been in a down sloping tight trading range for the last 2+ years. Traders expect this to continue which means they'll look to sell rips and buy dips until it stops working.

Put this one on your radar. Watch it to see if there's any follow through indicating a changing of regime.

Our swing trades we entered last week in Bollore (BOL) and Rolls Royce (RR.LN) look likely to be stillborns, reversing soon after our entries. We should know by Monday if they can hold the line or if we'll be cutting for a small loss.

Brandon and I are working all week on the reintroduction of the monthly MIR report which we plan on getting out to the group by week's end. We'll be diving into the world of changing energy trends, deglobalization, and where the two intersect to create some incredible deep value opportunities.

Shoot me an email or hit me up in the CC if you have any questions.

Your Macro Operator,

Alex