THE National Investor

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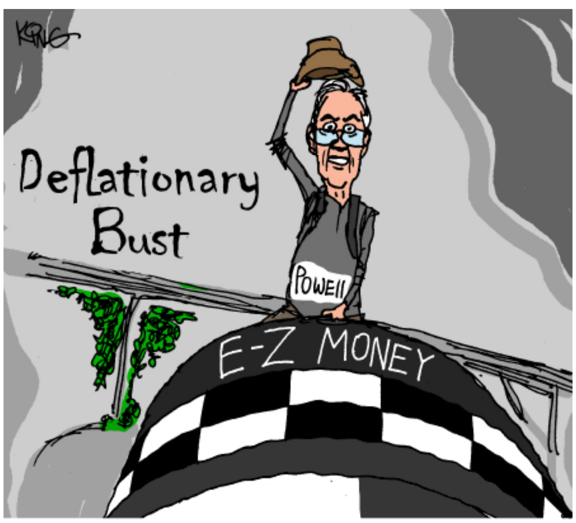
# MORE ON STRATEGIES FOR 2020

## THE FED RETURNS TO BUBBLE-BLOWING




Dr.StrangePowell (Or, How I learned to stop worrying and Love the Bubbles)

In my second issue of January, 2018—at a time in more respects than not similar to the present moment, as I'll be discussing—I quoted a then-current opinion piece from *TheStreet.com* which held, "You can't reason with a steamroller." Coming on the back of 2017's powerful market, I added then, "…nothing seems to be able to derail one of the great stock bull markets of all time.

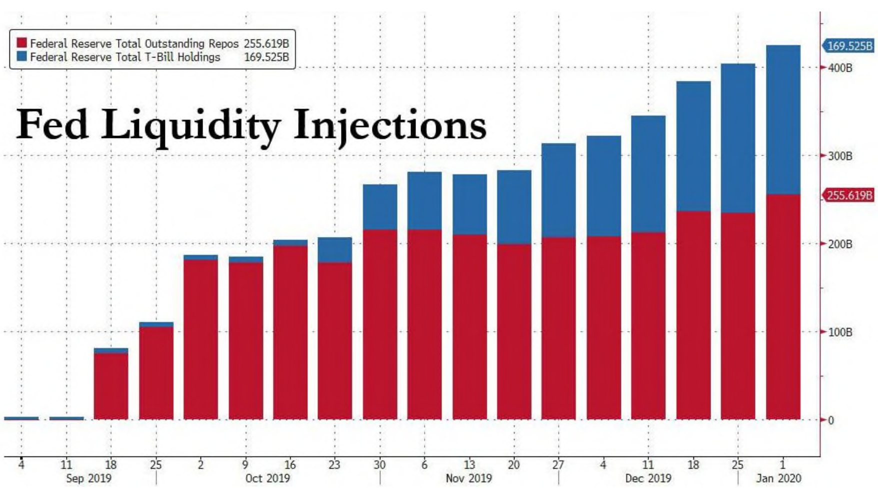
"That a stock market which is not only historically expensive but also historically 'overbought' technically needs a pause goes without saying," I continued. "Yet among the near-universal bullishness (voluntary or, increasingly, begrudging) even those near-*pining* for one look to any coming correction as one where investors will be able to 're-load' for the next push higher…"

**Next, we had a nasty two-phase correction**; one which—together with that of December of that year—led to the net result being a down year for stocks in 2018. One of the causes of the first episode (and what the second one ultimately *ended*) was the perception that newly-minted Fed Chairman Jerome Powell was going to follow through with his promise to systematically "normalize" Fed policy via both increases to short-term interest rates and reducing the Fed's bloated balance sheet. Powell often—*and quite correctly*—pointed out that the two most recent major recessions were caused by the Fed *first* allowing bubbles to get so large that they led to imbalances of various kinds, undue risk-taking and the inevitable bust. He insisted he did not intend to preside over a third episode.

***So much for that.*** Though President Trump incredibly *continues* to publicly chastise Powell, the FACT is that no single factor is more responsible for the record stock market. . .and the greatest economy in the history of the solar system, to hear the president describe it. . .than the Fed's abrupt and augmented reversal of course starting last year. And if anything, the Powell-led central bank will in the year ahead most likely deliver even more "help" for the markets and economy, not to mention the reelection chances for Trump.


On the interest-rate front, one of the more unsung aspects of late in Powell's shift to that *"Volcker, Part Two" mode* I have described (for some added background on this for those who didn't read it previously, check out [https://nationalinvestor.com/2168/the-fed-and-your-money-in-2020-volcker-revisited/](https://nationalinvestor.com/2168/the-fed-and-your-money-in-2020-volcker-revisited/)) is **his recent re-characterization of those three "insurance" rate cuts of 2019.** Though we now have both the U.S.M.C.A. signed as well as a "Phase One" deal with China (dubious in its likely benefits, but the markets don't care about that right now), a good part of the "uncertainty" that was used as a justification for those cuts is now gone. Yet Powell has recently told us that they are here to stay.

**Then we have the "Not-Q.E." since those September's liquidity issues that suddenly beset the repo markets.** As I and others have been chronicling along the way, this has led to a more rapid growth in the Fed's balance sheet than anything previously seen; well over $400 billion since September. And even though a good measure of those short-term fixes do—*as of the moment*—seem to be unwinding (with the Fed's assets *dropping* by $40 or so billion the last couple weeks) the monthly buying of (last count) $60 billion of short-term Treasuries is continuing.




Unlike what was the case in 2018's almost year-long return to a little sobriety, **there is virtually no chance of the Fed being a negative factor in 2020.** In his last couple of major public pronouncements on the subject late in 2019, Powell set such a high bar for any increases in interest rates as to all but guarantee that there will not be any anytime soon for *any* reason, save "inflation" getting much hotter, and for an extended period of time. *Don't hold your breath for that.*

**The odds of that are still long, as I will be explaining farther along.** For that matter—as I just wrote in a guest piece on "The Flation Debate" for my friends at *The Prospector News* in their new issue's cover story (at [https://theprospectornews.com/](https://theprospectornews.com/))--DEFLATION is in the near term a far more likely outcome. To his credit—and, of course, with the simple mathematics of a stretched-to-the-breaking-point fractional reserve system working against him—Powell is attempting to get out in front of this and at least soften the coming blow. Whether he succeeds or not remains to be seen; and a Black Swan event such as the new coronavirus outbreak or something else out of left field may take it all out of his hands anyhow, at least for a while.

Such one-off events aside—and as I discuss this current weekend on the *K.E. Report's* weekend show (see http://www.kereport.com/2020/01/25/hour-1-7/; I'm on Segment two)—the broader new messaging from the Fed is about to get a boost. **Already, Powell and some others have increasingly been floating various ideas to try to get "Inflation" (in this context, of course, broader consumer and business price increases as opposed to inflating asset prices) perked up in a bigger way.** That there is a *need* for this to make ever rising debt levels a bit more manageable is indisputable, as I discussed on that above podcast. That the Fed will be any more successful than have either the Bank of Japan or European Central Bank to this point in this quest is a different matter.

*"Whatever it takes, I'm going to make it to the top!"*

**But an attempt will be made**; one which—Powell and Company fervently hope, I'm sure—will come *before* it MUST as an answer to the next deflationary bust. And as I described, the sales pitch for what is to come is about to be augmented as the markets, lawmakers in Washington and others learn more about why President Trump just (finally!) nominated Dr. Judy Shelton and the St. Louis Fed's Christopher Waller to vacancies on the Fed's Board of Governors.

That new ways must be devised to justify ever-more creation of DEBT and ever-more boosting of bubbles of various kinds is a given. **But—as I wrote in these pages several months ago when Shelton's and Waller's names were first floated—what we are in store for is something beyond the E-Z money regimens, Q.E. and all the rest of the last dozen or so years especially.** Waller will put one of the most "populist" faces on his vision of monetary policy of anyone appointed to the central bank in recent memory. Much of his work at the St. Louis Fed revolved around coming up with new ways to rationalize the "new era" of monetary policy Waller believes we are in; one arguing for *permanently* lower interest rates. Importantly—and in a fashion that will benefit Trump *politically* as much as anything—his approach to monetary activism will resonate with the middle class and those neglected by past Feds who simply showered Wall Street with free money.

***Two fresh and more articulate nominees. Same "Inflate or Die" agenda.***

As for Dr. Shelton, she can be compared to another past personage—in her case, to former Fed Chair Alan Greenspan—who once was purportedly a "gold bug" and sound money advocate as well. **We know how he ended up, however, due to the need to make the elastic, fiat dollar endlessly more so: as I have described him, the single most-destructive policy maker in American history**. The man never met an unregulated derivative or crackpot securitization scheme he didn't like, turning both Wall Street and the banking system ever more into frenetic casinos.

Shelton remains enough of a "rock star" with conservatives and sound money people that she will probably do well (as her born-again monetary activism *present act* wins over Democrats also) despite—as Mises Institute personage and economics professor/writer Joseph Salerno just quipped—her stance being essentially "I favor sound money—and plenty of it." (For his opinion piece on that organization's web site of this past week see https://mises.org/wire/fed-nominee-judy-shelton-wants-sound-money%E2%80%94and-lots-it?utm.)

***Both* of these nominees will likely make more legitimate in many folks' eyes the transformation of the man who nominated them on such things.** Lest you have forgotten, *Candidate Trump* was the one who warned that the Fed had blown unsustainable bubbles—especially in the stock market. *President Trump* continues to carp about the Fed not rewarding him as it did his predecessor with such monetary activism. Indeed, as he told *CNBC's* Joe Kernan this past week at the World Economic Forum in Switzerland, the Dow would be as much as 10,000 points higher still, and G.D.P. growth at 4% instead of half that, were it not for Jerome *Scrooge*.

More than the *actual moves* near-term on monetary policy the Fed may engage in (which are likely to be on the "dovish" side, though a "hiccup" may be in store as the repo operation unwinds some) **I am going to be paying rapt attention to the upcoming confirmation hearings for Waller and Shelton.**

## STOCKS IN 2020 SIMILAR TO 2018 *ANYWAY*?

Notwithstanding the fact that the Fed is *unlikely* to be part of the problem this time, simply due to the facts that 1. We are starting from an even more overextended place than in January, 2018 and 2. There are numerous risks—known and unknown—before us, **my "base case" expectation *currently* is that we will have a *very* choppy year such as back in 2018.** And to boot, the twists and turns of how the looming Election season is shaping up will make things more so.


While there has been relatively little quibbling over the idea that stocks *generally* are overvalued (with many conceding the "answer" is simply—as with Powell—to stop worrying and embrace the fun) **the week just ended gave at least some of the smug bulls pause to wonder**. Now—on the back of still-mixed economic news in the U.S., added signs of stagnation most everywhere else and the rest—we have *added to that* the Coronavirus outbreak.

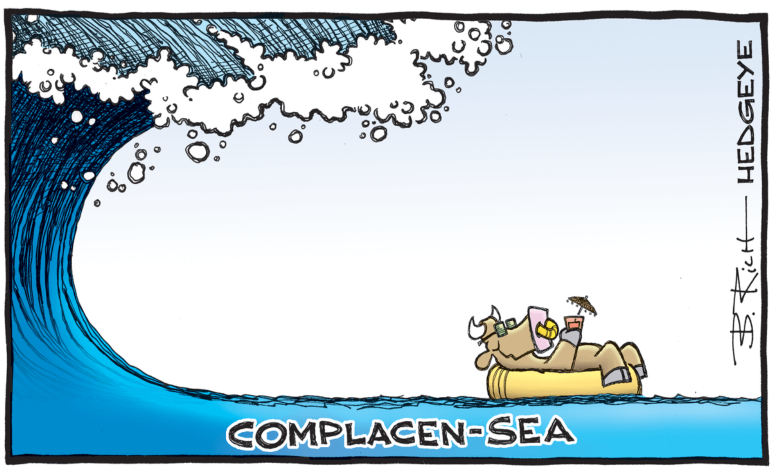
I'll have more to say on that new "Black Swan" a bit below. **For present**

**purposes, stocks gave a glaring sell signal at Friday's close, chiefly over worries that a substantial spread of this new virus will *meaningfully* upend economies and markets, mostly in *already-shaky* China.** In what is in technical parlance an *outside day* or *outside reversal*, stocks first exceeded to the upside the best level of Thursday, before reversing and closing below the *lowest* trading level of Thursday. Such reversals typically are evidence of an *especially* abrupt change in attitude; one sufficient, at times, to lead to a broader correction especially when things are *starting from* such lofty levels.

Even if we are *finally* about to get an overdue correction of some consequence, that means neither that we are going to have an election-year *crash* nor a repeat—even if I am wrong about a near-term correction—of a 2020 melt-up as strong as 2019's. Frankly—as I will be describing via numerous factors below—I see arguments for just about anything; *but in the end, a flat to slightly down, choppy year for the market even if the risk of a more momentous "crash" is ever present if enough things go wrong at the same time.*

Many of the items below I'm going to be expounding on in the days and weeks ahead. For present purposes—and because I want to save time/space for some general thoughts on what we are/should be *doing*—I am going to move fairly quickly.

## BULLISH ARGUMENTS/FACTORS




-- **Momentum, policy and the "TINA" Factor** – When such skeptics of the recent mania as hedge fund manager Stan Druckenmiller and Paul Tudor Jones even concede that (in my characterization) you simply have to hold your nose and join the buying, it's attention-getting. Sure, as Jones concedes, this will all lead to an epic blowoff top one of these days. But between now and then, the old adage that "The market can remain irrational longer than short-sellers can remain solvent" will continue to hold sway.

Indeed, as another skeptic of the *fundamental* foundation (or lack thereof) of the market's rise—Ray Dalio—added this week, simply, "Cash is trash." **The Fed has consciously rendered it so for a few reasons**: where the present discussion is concerned, so that everybody will embrace that "There Is No Alternative" mantra and push stocks (and other assets) to the moon to keep the whole skyscraper of cards from falling.

As Jones explained in an interview (see [https://www.cnbc.com/2019/11/13/paul-tudor-jones-says-there-is-an-explosive-combination-of-forces-driving-the-market-higher.html](https://www.cnbc.com/2019/11/13/paul-tudor-jones-says-there-is-an-explosive-combination-of-forces-driving-the-market-higher.html)) virtually every factor possible has been aligned in favor of the melt-up in stocks (as well as other financial assets.) Explained Jones, "We've got a 5% budget deficit coupled with the lowest real rates that you can imagine with the economy at full employment. That's the most unorthodox, and potentially explosive, combination that you can imagine. It's like the photo negative of 1930, when we had the last trade war, but you had tight fiscal and tight monetary policy. Now we have the exact opposite."

“We’re in such extraordinary times,” he summed up. “We’ve never seen a fiscal and monetary mix like this. So it argues for some massive blow-off at the top.” ***When*, of course, he didn’t speculate; nor can anyone, hardly.** A few cautious folks (in the sense of NOT advocating heavy bets against the market, even now) remind us that the Nasdaq *more than doubled* from 1999 until its blow-off peak in 2000. And that, of course, was despite the many gasps along the way as the market’s valuation fundamentally became increasingly unmoored from reality. *It didn’t matter*.


**-- The U.S. Dollar (IF—and that’s a big IF—it *really has* peaked.)** For a little while there, it sure looked like the greenback’s occasionally meandering but well-defined uptrend was finally going to be broken. And as I have long been pointing out, it’s the strong dollar that has been *strangling* emerging markets and foreign debtors.

The Fed has at least tried to do its part. As you see on that nearby chart, in fact, **the dollar’s peak of last fall more or less coincided with its “plumbing” intervention in the repo markets and beyond**. I said at the time that you would know whether or not the Fed’s actions were successful IF YOU SAW THE DOLLAR DECLINE. And it did.

Yet another thing I am curious to see/hear is what if anything the Fed has to say about the dollar at this coming week’s F.O.M.C. meeting. That in turn will probably be related to what Powell has to say about ongoing repo market and other actions. *The risk*—with the euro fundamentally and technically weakening anew and the chance that the risk-off sentiment of this past week drives the dollar higher—**is that the greenback gets away from Powell and *spikes*.**

The dollar’s softness of the last few months has had a lot to do with relieving stress in global markets as well as boosting U.S. stocks. More weakness—if it comes—will do likewise.

**-- China’s currency –** Related to the above, of course, is that the Chinese yuan has had a decent rally against the dollar since its worst levels of late last year. Aside from the relatively more mundane meaning that carries for merchandise trade back and forth, **it more importantly takes some of the pressure off of China’s financial system and markets.** Still-looming *disasters* from debt dominoes falling and renewed capital flight are possible; and likely still just a matter of time. But all else being equal, those who want to continue to flog the bull case for the global economy, etc. will be cheering even more dollar weakness/yuan strength.

-- **No negatives from trade, etc**. -- As I quipped above and have discussed a bit recently (and will be again soon) that Phase One “deal” was FAR mostly about politics, salesmanship, massaging markets and B******T. But that doesn’t seem to matter (yet); and if we can manage to get through 2020 *without* too much evidence being revealed of what a sham this thing is for the most part, that will be a positive.

In addition, it's seeming as if Trump is *trying* to defuse looming spats with Europe over taxes, trade, etc. as well. If he can manage to maintain the status quo—and all else being equal—he will have the *appearance* at least of having succeeded in what at times has been a belligerent approach to trade wars. And that will benefit him more than not, as well as further remove any angst over such issues from the markets.

**-- *Even more* stimulus?** -- Trump and his chief economic cheerleader Larry Kudlow have on several occasions (and anew) suggested they will push a "Tax Cuts 2.0" agenda *this year*. I don't see a House controlled by what will STILL be a very angry Democrat Party cooperating on *anything* much. But the more Trump pushes this and the more T.D.S.-afflicted Democrats hysterically push back, the greater the odds will be of a second Trump term AND a comeuppance for Democrats in the House and Senate too.

-- **Business/markets DO believe Trump will be reelected –** That is a *big* part of the reason for the level of stocks now, right or wrong…and bubble or not. I would say that, in addition to the dollar needing to stay tame, the prospects of the president's reelection (or not) will be one of the biggest drivers of the markets this year.

## BEARISH FACTORS/THOUGHTS

**-- Valuation. . .and valuation! --** *Fundamentally*, stocks have *never* traded as high as they do now in comparison to their sales; see https://money.com/stocks-price-to-sales/ for several examples and anecdotes. They are in nosebleed territory too in relation to earnings (and *massaged* earnings at that.)


The T.I.N.A. argument and the corollary one of interest rates being so low as to make a much easier comparison for stocks are valid *to a point*. But eventually, there needs to be some—*preferably strengthening*—underlying cause to believe such valuations can be supported.

**-- Corporate profits *don't* rebound? –** The last two years have really turned some traditional "playbooks" on their heads, especially where earnings are concerned! In 2018, the Standard & Poor's 500 was *down* about 6% despite strong double-digit growth in corporate earnings (albeit, goosed by the Trump tax cuts.) Last year, the S&P 500 was *up 29%* even as corporate profits ended the year with pretty much NO year-over-year growth. *Of course the Fed "helped" both ends: its actions were negative for stocks in 2018 and positive in 2019*.

The present belief in the markets is that Corporate America will be back to double-digit growth in 2020; at least by the back half of the year. That is presently the bar over which results must leap. . .or fail to reach. **So the current earnings season is every bit as much a look ahead as it is behind; much more than usual.** I personally *don't* expect as good a result of things; and if I am correct, that will be a negative as the year progresses.

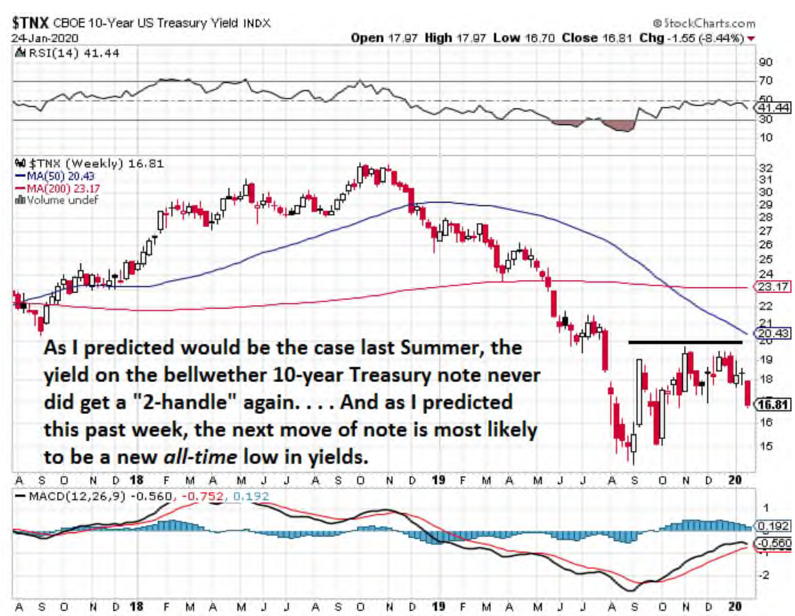
Here, however, **IF the dollar has peaked**—and preferably softens further, finally breaking that upward trending channel—then the odds of dour corporate earnings turning from a bearish factor to bullish will be enhanced.


**-- Corporate bonds deteriorate and lead stocks lower** -- In just the last few days, a potential harbinger of a correction for stocks even before Friday's outside day was **the acceleration in the woes for junk bonds.** By no means a disaster yet, flare-ups over credit worries and economic health of the last few years have at times repeated the same pattern: junk bonds (represented at left by the ETF, HYG) swoon and drag stocks with them.

Especially now—**and especially with weaker corporate credit, where a muddle-through economy IS NO LONGER ENOUGH to *even service* debts that are too onerous**—the markets are at risk from an increase in defaults (already underway but still low historically), weaker economic growth, the need to refinance **and RE-RATINGS**. I'll especially be talking more soon about the last of those. Don't forget that one of the consequences following the 2008 bust was a lot of punishment meted out to analysts, ratings agencies and others who basically lied about the health of the paper they opined on. I don't think markets are prepared for the numbers of downgrades and the associated pain of (or inability to garner) refinancing that lies ahead in a world where low-rated corporate credit has for a while already been a ticking time bomb.

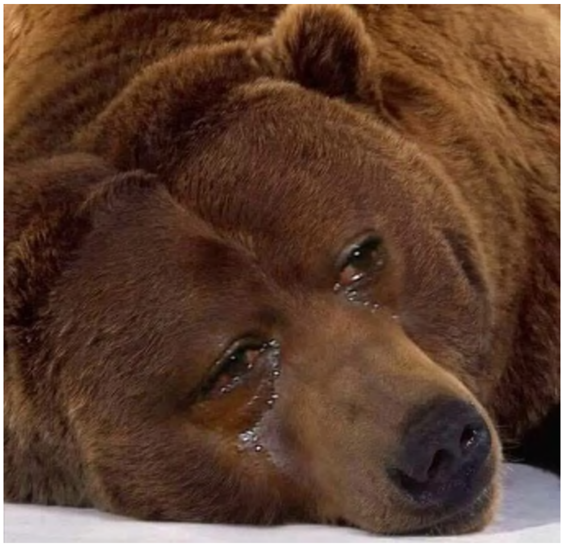
**-- Commodities rolling over again** -- Even before the worry over the coronavirus outbreak made things even worse in the last few days, industrial commodities and energy were *already* rolling over following their brief pops. *Crude oil has been absolutely annihilated*; I'll talk more about it below. Commodities *generally* I will be discussing over the next couple issues.

For present purposes—and as I discussed (*especially presciently*, it turns out) earlier this week in describing stocks as the only outlier when almost every other asset class is *screaming* recession and deflation dangers—the breakdown in crude, breakout *failure* of copper and more ALL point to an economy sicker than is believed, *and thus a stock market with a lot of air under it.*




**-- Interest rates rolling over, too --** That the bellwether 10-year Treasury note couldn't even make it back to 2% recently (let alone the 3%+ high of 2018) despite a LOT of reasons many say it should have tells you *a lot*.

And what it *continues* to tell ME is that 1. U.S. paper STILL has demand from overseas *given outright negative nominal yields elsewhere*, 2. It is LAUGHING at the newest Powell claims of trying to stoke more inflation, 3. It is likewise laughing at The Orange Wonder's claims of the greatest economy in all of recorded history and 4. Its momentum might take it *even faster* than I already expect to new all-time low yields, especially if the coronavirus outbreak REALLY starts to give markets the willies.

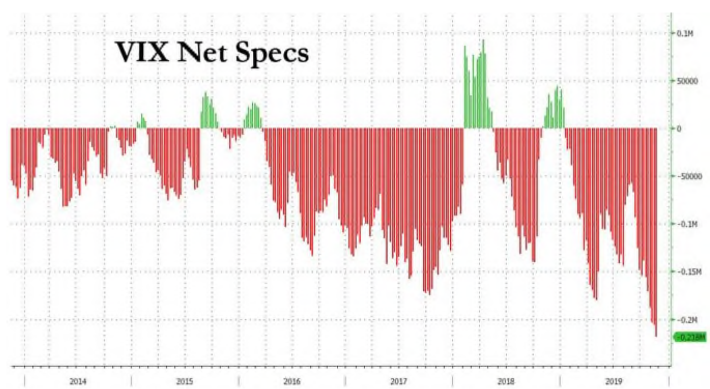


Simply put, were much of the bullishness toward stocks especially remotely warranted, long-term yields would have *kept rising* as they started to do late last year. **Here again—similarly to what has happened to oil, copper et al—bonds were already rallying and yields falling *before* the coronavirus outbreak.** Suddenly, I heard a few pundits this past week correctly—for a change—paint this drop in market yields as a VERY bearish development (at least for overvalued stocks and unrealistically Pollyannaish economic growth expectations; I'll explain where they are GOOD below.)

True, our friend there on the left has felt *very* alone and unloved for a while. But that will begin to change *a bit* as I think the bears have *by far* the better case fundamentally.

## WILD CARDS / BLACK SWANS

* *Near-term* the most acute danger is the kind of **liquidity issue** that rocked stocks two years ago in that two-phase, brief beating meted out in early 2018. As then**, traders have been shorting the VIX**; as you see at right, even more as 2019 ended than before. By extension, they go **long stock index futures** and/or the largest cap stocks that—as many have been pointing out—are as absurdly priced now as the "Nifty Fifty" of old.





We saw what happened two years ago when all that unwound pretty much in one fell swoop. Today the dangers are greater *and even more concentrated*. It's appropriate again—perhaps as we are on the edge of the latest liquidity traps being sprung on complacent investors—to remind you of how the minnow/bait traps of my youth operated!

**Or in the words of lyrics to The Eagles' great hit Hotel California, "You can check out any time you like, *but you can never leave*."**

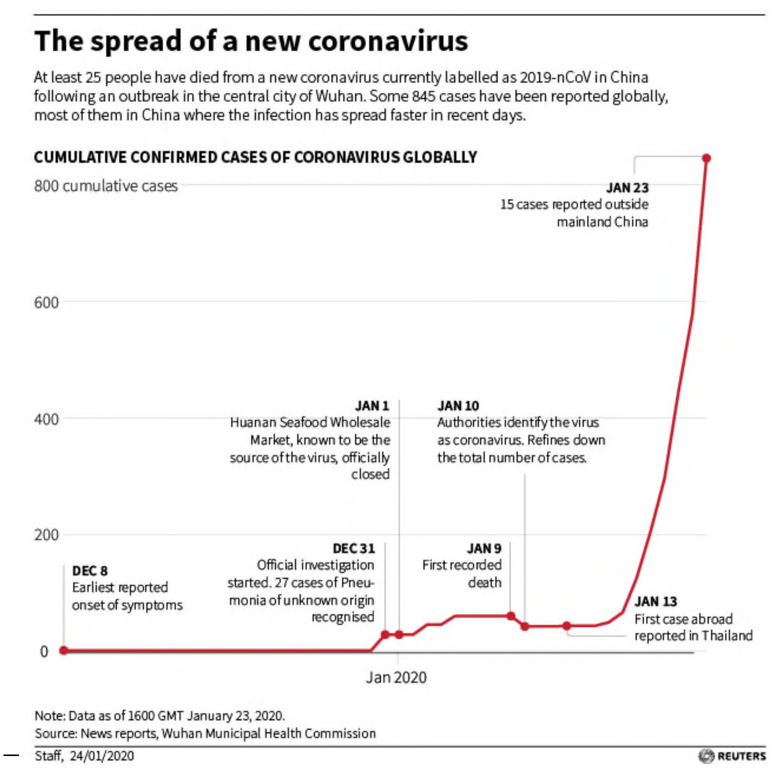
This danger has become greater across the board, in fact: not only for stocks, but for wide swaths of corporate credit. In either, once the Greater Fool Theory has played itself out and there are no buyers left, *who are the last buyers going to sell to*?

So that ever-present danger is especially noteworthy now, even if it manifests itself "only" in a brief but nasty "Flash Crash" – and that is **a market event** punctuated by a sudden lack of liquidity and maybe even (unlike, thankfully at the time, 2018) a seizing up of basic market functioning.


* **Emerging markets** are still quite shaky in many respects. Here again, much of it is due to so much **unsustainable debt** having been taken on (much of it in U.S. dollars no less, I hasten to remind you) that far from ever being able to pay it off, there's growing stress in *just servicing* it all.

And here, too, markets could be blindsided in the coming months if a big slug of such debt has trouble being refinanced.

Institute of International Finance President and C.E.O. Tim Adams warned of this in the past week; see https://www.cnbc.com/2020/01/23/iif-chief-warns-of-white-elephants-amid-record-global-debt.html. Besides the ugly stories told by the raw numbers themselves there is the question of the shady nature of how some of this has been characterized / rated in the first place.




* **I've said for a while that an unexpected shock to markets is far more likely to originate *outside* the U.S.** An emerging market crisis is most always possible as an exogenous or "Black Swan" event. So too with Europe and (Number One *still*) China where banking and related issues continue as BIG accidents waiting to happen.

* Nobody, though, could have or did predict **the newest coronavirus outbreak**. Worse, central banks have no more of an antidote to make it go away right now than does medical science. *Worse still*—and unlike the 2003 outbreak, the most recent such event that did measurable damage to (chiefly) Asian

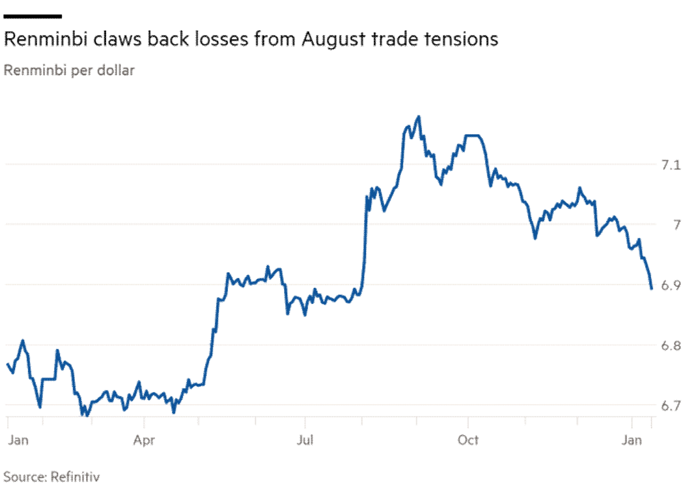
markets and G.D.P.—this one comes at a *far more vulnerable* juncture for Asian markets and economies in particular.

First off, that this outbreak hits at the beginning of the Lunar New Year is **devastating for economic activity at the heaviest time of year**; and it arguably negates all the good that had come from the recent yuan strength, less worry over trade, etc. Chinese, Hong Kong and broader Asian markets got hit fairly hard this last week on those worries; and *more is likely to come*.


*Geopolitical Futures* wrote this past week that even if this outbreak is *medically* not as bad as the 2003 SARS one, the effects could be *worse* on a Chinese economy already under such stress to hold things together that there is NO room for error. "The costs add up quickly," they wrote in speaking of the sudden grinding to a halt of travel and other economic activity. "The SARS outbreak in 2003, for example, dented Chinese gross domestic product by as much as $30 billion, reducing growth by near 2%. Globally, the bill for the pandemic ran up to as much as $100 billion. . ."

". . . even if nCoV proves more manageable than SARS, there are reasons to think the impact this year will be worse. For one, the SARS epidemic occurred on the heels of the dot com crash, when consumer spending across the region was already somewhat suppressed. (Incidentally, the resulting reduction of international travel may have helped contain the spread of the virus.) For another, locking down an urban area as large as Wuhan – a city at the center of one of China's most important internal shipping routes along the Yangtze – will be immensely disruptive. . .

". . .The biggest difference for China this time around is that the economy can't as easily shrug off a major shock. In the early 2000s, annual GDP growth was still climbing well above 10 percent. Today, with a long structural slowdown well underway, Beijing is running up staggering debts just to keep growth from swan-diving below 6 percent. Add to this an unresolved trade war with its largest export customer – along with its scramble to implement critical but growth-sapping measures to stave off a financial meltdown before the next global slowdown strikes – and the epidemic starts to look like the sort of thing that could derail Beijing's best-laid plans for avoiding an economic reckoning."




The healthy rally in the Chinese yuan from last summer—to *below* 6.9 yuan to the buck, from around 7.2 prior—**abruptly reversed this past week.** Needless to say that bears watching. As I quipped this past week, the appearance is that market strength is a mile wide. . .*but it's only an inch deep*. Added to a lot of what I have been discussing above, fears over this coronavirus could have a domino effect. . .and lead to the next round of liquidity issues, flash crashes or whatever.

# SO WHAT DO WE DO. . .AND NOT DO?

On pretty much each and every of the following subjects, I'll be providing added thoughts and recommendations to Members following this issue; in some cases, *imminently*. For now I am going to stick with a broad *but brief* "road map" of *generally* how I advocate themes and sectors being apportioned:

## TO SHORT, OR *NOT* TO SHORT? THAT IS THE QUESTION

In 2018, with the S&P 500 down about 6% for the year, our average portfolio was UP by 21%. And a fair chunk of that nice outperformance was having perfectly traded into both "phases" of the early 2018 correction via inverse ETF's, and later getting the majority of the late 2018 swoon logged that way as well.


But in 2019, with the S&P 500 up a sliver shy of 30% our average portfolio was *up only 19%;* and we were saved late in the year from an *even worse* underperformance by several individual stocks having big, late-year surges. **The advocacy of mine since especially August 1 to take somewhat bigger stakes in our usual inverse ETF's clearly did NOT pay off yet, and dented our overall performance for the year**.

Between the Fed acting pre-emptively to *at least postpone* the next deflationary spiral downward AND the Chinese yuan's rally slowing capital flight over there for now, **the *systemic* issues I saw as clear and present dangers were mitigated**. But they are still there; and as I'll be explaining in a follow-up to this for Members, I am looking at how to more than make up for that recent underperformance due to our inverse ETF positions, while still acknowledging what has been *until now* the overriding heavy hand of the Fed to keep the stock market propped up.

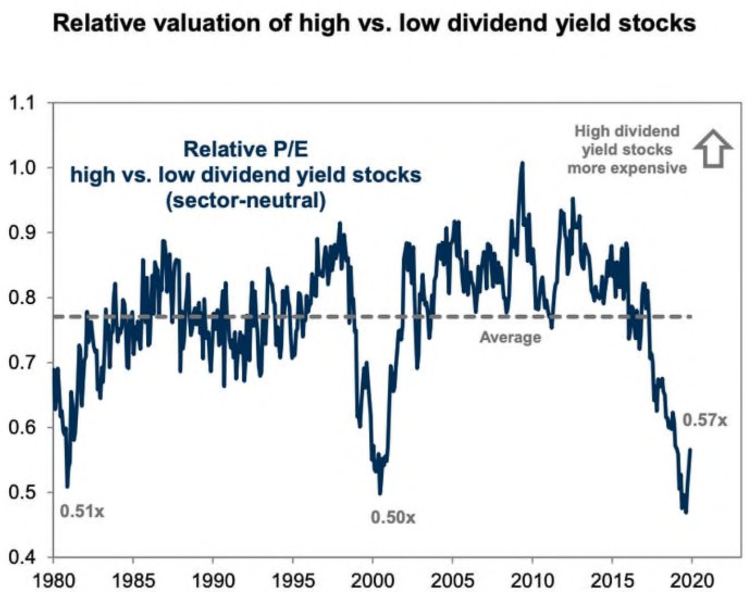
As the nearby chart shows, it is what have been the strongest of the big caps and momentum stocks (Tesla more than doubling in *weeks*…really??) where the biggest risk will be if money managers get nervous and start wholesale reversing trades. The question will be whether *everything*—overpriced and cheap alike; growth and value alike—falls in a Flash Crash, were that to develop, or whether we can make money "long" value, yield stocks, gold, etc. *even as we simultaneously make money shorting elsewhere*.

Stay tuned…

## WHERE DO WE WANT TO BE "LONG"?

* **The Safest bet: Falling yields –** If nothing else, correctly anticipating some time back the renewal of the secular bull market for Treasuries that is soon to close out its fourth decade, we established our heaviest-ever positions in ETF's directly or indirectly playing on the rise in Treasury

prices/fall in long-term market yields. And as I argued above, that posture is very likely to continue rewarding us. Indeed, as I discussed back in my first discussion of the year both on the K.E. Report and on Benzinga.com's Pre-Market Prep Show, the one "prediction" I was most certain of looking ahead was that the rise until then in long-term interest rates was OVER.




By and large—albeit with a few exceptions—our **Income-oriented stocks** have done well for us also, *though their ranks remain a bit light for two reasons*. First, I felt it wise to sell some for various reasons in recent months (in almost every case, at or very near what ended up being highs.) Second, yield and value stocks have been generally bad laggards (though with a few happy exceptions we've benefitted from) as the oceans of "passive" money have again been chasing the "mo-mo" stocks higher. Third—and especially where a number of high-yielding energy stocks I'd like to add back/recommend anew are concerned—I'm neither a bull nor a bear but *a chicken*.

In a perfect world (meaning for this specific discussion, entry points into more of these kinds of stocks) I'd like to see that "Flash Crash" develop…knock *everything* down a bit…galvanize the Fed's new dovishness…and ***force*** **investors to choose yield and value over the dopey valuations they have been chasing in the largest cap growth stocks, etc.** Were we to get all that—or some other combination of factors I like—I'll be adding *several more* yield stocks.

*** GOLD a winner in pretty much any scenario –** The other half of the storied "Odd Couple" has remarkably been hanging right at that key long-term technical level around $1,550-$1,575/ounce recently despite some reasons skeptics say it should *not* have.

You had the stock market continue toward record highs which *should have* dulled gold's luster more. Ditto the Phase One trade deal signing and ostensible removal of *that* as a market worry. You have central bankers from Powell to others crying that there isn't *enough* inflation (a key factor four decades ago for gold's 1970's run but WAY less relevant today.) And on it goes. . .

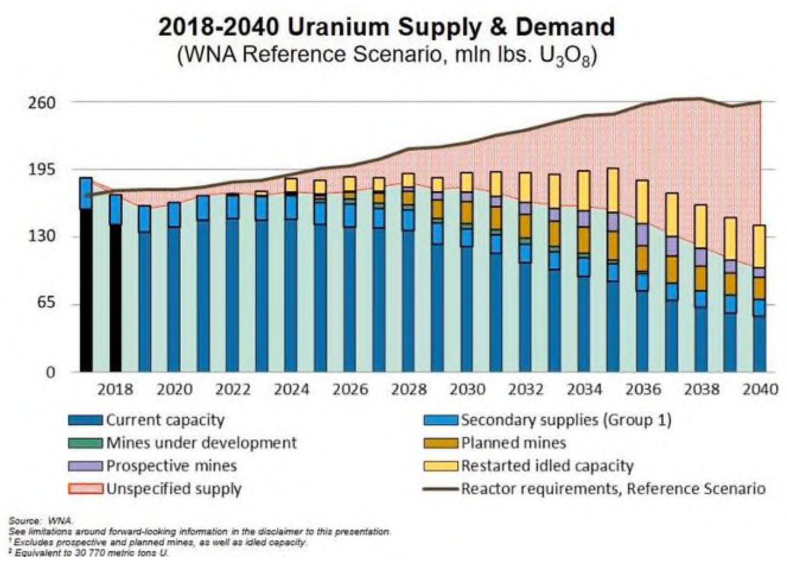

**In fact, it's been DEFLATION worries in the past year that have led to gold's surge.** As you see in the nearby chart, gold has fairly closely mirrored the rise in the levels of negative-yielding debt globally. *It is, as I have been calling it, the "un-currency."*

Mining stocks have been doing well also; both the ETF's we have also been heavier in over the past year (though still scarcely half our peak allocation of late-2010 and early-2011, when I recommended—again, presciently as it turned out—that we start cutting back) **and individual names**. Where *the latter* are concerned—as I will be explaining more also in an issue quickly following this one—a refreshing development is that most of the "garbage companies" are NOT participating. *And that's good.*

I've already identified one of my 2019 additions as THE company most likely to supplant **Sarepta Therapeutics (NASD-SRPT)** as my No. 1 all-time winner. In the next issue I'll have a fresh update on the 2020 exploration agenda for another that could hit its long-awaited "home run" this year.

*And also not many days hence I'll be adding my latest individual company in the gold space to my recommendations as well.*

About the only thing I see ahead that *could* render gold somewhat of an under performer is if we get a more sizeable drop in the dollar's value for some reason *in the context of more traction for the global reflation narrative*. Such a "Stagflation Lite" environment as I have mused about from time to time, though, would only render gold somewhat of a laggard (though I still see it doing well) because base metals, energy, cyclicals et al would FINALLY get more sustained attention.




* **Uranium an outlier with its own unique fundamentals** – Of pretty much any key metal/commodity you want to name, I can't be convinced that there is a better case *presently* than for uranium. Other key ones—such as copper, and lithium and other battery metals—have great stories too; but ones I believe are going to take longer to develop and/or be more safely "investable."

As I explained in the 11-minute introduction of my latest addition in this past week's webinar, **the global growth story for nuclear-generated energy AND the corresponding screamingly bullish supply/demand factors for uranium *should not be ignored***. (BTW, if you missed that, go to https://register.gotowebinar.com/register/6774249872076707841.)

* **Other stories as the U.S. focuses on "strategic metals and minerals."** – As many of you already know, *part* of the bullish story for U.S.-centric uranium companies in particular are the looming measures by the Trump Administration to reclaim some long-lost leadership in nuclear energy technology **and to bolster domestic sources**. But though this has been one of the highest-profile stories as the Administration *correctly* looks to addressing vulnerabilities due to imports, *it's not the only one*.

Following both the spirit and the dictates of, in part, a Defense Department report identifying numerous minerals, metals et al where the U.S. is vulnerable to too-heavy a reliance on imports, the Army recently announced it will co-finance **a rare earths recovery facility in California**. Members already know that my latest pick in **the lithium space**—though I remain ambivalent about that weak mineral's outlook *near term*—is due to that company's **U.S.-based** asset that is the most compelling of its kind in America.

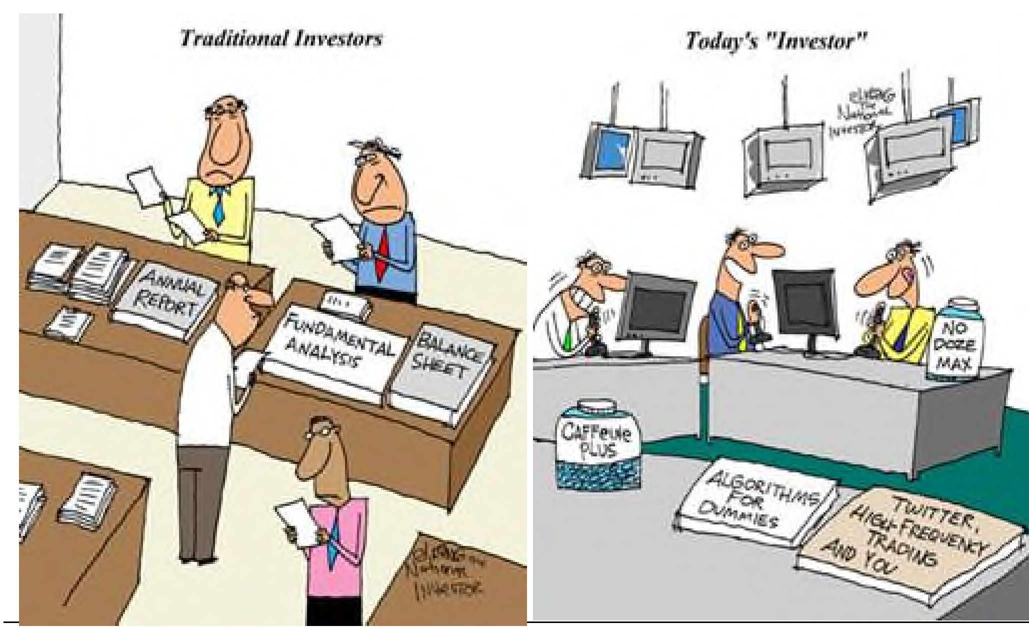
And helping undergird the GREAT story for my only other—and oldest—lithium pick (which we logged a 700% profit on a couple years ago *and is an even better company today to be in*) the cooperation on metals and energy just announced between the U.S. and Canada is *very* bullish.

I'll shortly be adding such companies that meet this theme.

* **Biotech stocks –** Notwithstanding any of the above, no sector sports companies as rewarded for *individual* merits and good news as does biotech. We've enjoyed numerous successes over time; none more, of course, than Sarepta. And in addition to it still and a handful of others of various kinds on my list, expect to see more additions here before long as well.


* **Value stocks *generally* –** I am not the only one who has alternately predicted *and pined for* a saner environment to return that would finally "reprice" stocks more for their fundamentals. As you see at right, *Barron's* has on and off predicted the same; this cover, though, from *nearly two years ago*.

We've had some success here in picking off good, solid and even dividend-paying companies even in an environment where passive investing is still holding sway: a few of the more notable names of companies too cheap at the time to ignore have been **Symantec**, **CVS Health** and **Big Lots** (the former two are now gone after nice profits were taken.)



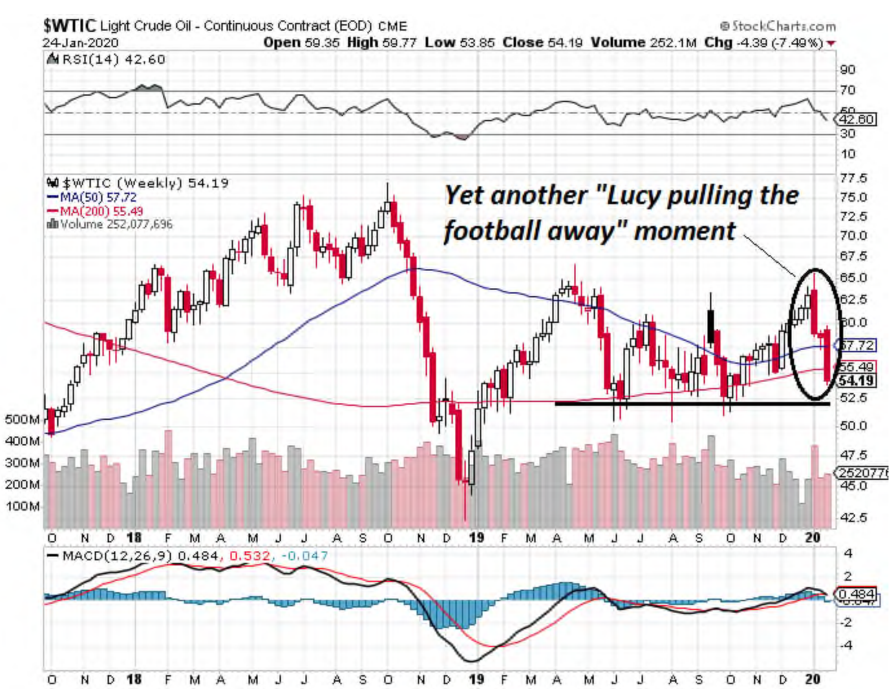

The kind of environment I see ahead *should* be conducive to value stocks making a long-overdue comeback. When the U.S. more notably joins the rest of the world in its own "Japanification," things should become more sober; and more conducive once again to *investing*.

In fact, tougher times ahead should actually be constructive for companies that are legitimate values, as opposed to the high-growth and momentum names that have become more lottery tickets than true value-oriented stocks (Apple even, for one, has *nearly doubled* during the same time that Y-O-Y sales are up a scant 2%.) My favorite statistic in this regard (some of you have heard this story) concerns the bear market amid the Great Depression. From the peak in September, 1929 to the spring, 1932 low, the Dow Jones Industrial Average plunged by 89%. Yet during that same time, fully one-third of all publicly-traded companies were *higher* in price.

I for one would welcome such an environment **where investors could act like investors**—and be appropriately rewarded!

* **NOT safe yet – Energy stocks –** One of my working titles for a near-term piece on energy stocks *had been* one suggesting they could be the "comeback kids" of 2020. I've lost count of the number of times since the *ugly* energy environment of early 2016, give or take, when there's been a "false start" for the sector only to see it result in even more weakness for what look like vastly undervalued companies. . .but instead have turned out to be *value traps*.


The truth revealed by the chart above has been well-covered by many: **chiefly, the historically low representation of energy as a portion of the overall market.** Part of that, to be sure, is the recent overvaluation of other sectors especially; no question of that. But it *also* underscores the misery that investors in this sector have experienced; even at times when oil has mustered a rally, rallies for energy-related equities, if they have occurred at all, have time and again reversed.




This month's *brutal* beating for energy bulls that were just thinking it was safe to poke their heads out again has been especially telling. With no reason for prices to follow through as the Iran issue turned out to be a quickly-passing "dud" (as an investment story, anyhow) **oil was already surrendering its move *even as stocks continued to rally*.** There is simply no getting away from the fact that there is STILL a looming and perhaps worsening supply glut; **and with natural gas as well**, which in the last few days managed to slip under $2.00/mcf for the first time in several years.

So we're right back to the environment I heard someone describe a while back as: "Oil stocks are about as popular as gangsta rap at a nursing home." The coronavirus outbreak *could* make things MUCH worse near-term as well; if economic worries or, worse still, a market shock in China/broader Asia materialize, **we'd see oil plunge to the late 2018 low in a heartbeat.** Then—maybe—I'll be a bit bolder in adding or adding back some companies I really like, but don't dare touch *now*.

*Longer-term*—as you will be reading a bit down the road—I am sniffing a broader opportunity for some investment of consequence back into conventional energy. *But the way it materializes is going to be gut-wrenching.* Again, that's a story for another day. . .

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