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My credentials are legit, I swear!

In a week of lies and disappointments, the market continued to run, hitting a high for the year.

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Things are not always what they purport to be, a hard lesson we learn as we get older. It now appears a late March Mar-a-Lago meeting between Presidents Trump and Xi to button up a trade deal is unlikely. That's disappointing. The president said talks were going "very nicely." Negotiating tactic? "I'm in no rush," said Trump. "We have other deals we are cooking," he said. "I think President Xi saw that I'm somebody that believes in walking when a deal is not done." Negotiating tactic? Secretary of State Pompeo said Wednesday that China is "in a league of its own" when it comes to violating human rights. Is this a negotiating tactic?? It's not unusual for negotiations to feel like they are winding down yet drag on for weeks or even months. Trump has made clear he wants a deal and has lowered the bar for what a successful deal would look like. However, because a weak deal could be a political liability for him, there is a real chance he could walk away as evident in his comments. Time arguably is of the essence, as the two presidents who lost reelection since World War II were the only two presidents with increasing unemployment rates in their election years. President Trump's economic approval rating hit its highest level of his presidency in February and is likely correlated to the boost in earnings and incomes, outcomes that in large part will require a favorable trade deal.

Lies and disappointments. Elsewhere, U.K.'s Parliament ruled out a no-deal Brexit, kicking that can down the road as Europe and the U.K. belabor the Irish border and other issues. Third Seven Capital suggests "one more misstep by May and the Tories could open the door to that armchair Marxist Jeremy Corbyn." Not much progress, and another disappointment. Yet elsewhere, it seems U.S.-European Union trade talks are at a "complete stalemate," as U.S. Trade rep Robert Lighthizer put it in his testimony Tuesday before the Senate Finance Committee; the two sides can't even agree on whether to include agriculture as part of the negotiations. The base case is Trump won't impose tariffs on cars or auto parts for at least the next couple of months, but there is a real risk he will, particularly if the negotiations continue to go nowhere. The White House has a soft May 17 deadline to make a decision. And Nafta 2.0 is running into serious opposition in the Democratic House and looks unlikely to be approved. Democrats say they don't like the substance of the reworked trade pact. Is this a lie? Or are they just unwilling to give President Trump a big political win. Now, I am exhausted.

Stop it, Linda. Let's think positive. As I write this, the S&P 500 is making a new high for the year! While Thomson consensus estimates currently show a Q1 earnings decline of 1.4% year-over-year (y/y), its estimates show a 5.2% y/y revenue gain for the quarter, a sign earnings estimates may be too low. Bullish. The NYSE advance-decline line made a record high on March 1, confirming the advance, while current sentiment indicators are neutral and far from depicting excessive optimism. Also bullish. Based on history, recent weakness in the high-beta shares that have largely fueled the market's advance can either maintain a positive slope as leadership rotates away from beta toward more fundamentally substantive names, or retest a recent low. It appears the former is the case, as the S&P is in the midst of pushing through well-established resistance in the 2,800-2,815 range. As for the credit sector, one underappreciated factor keeping it positive is the lack of debt growth compared to past cycles, which should add to the longevity of this cycle. With the S&P off to its best start since 1991, it is reasonable to expect a pause in the upward trajectory. But with the market trading at forward P/E of 16.5 and 10-year Treasuries yielding 2.6%, the actual risk-reward profile of the market is favorable. Everybody's talking about college application lies this week. Well, my creds are legit. You can check it out. You know, 35 years in this business have given me a tough Italian skin. I am lied to daily (stats say we all are, about 4 times per day, actually) and disappointed often. So when I feel my blood boiling, I'm naturally off to buy some shoes!

POSITIVES

- **It wasn't such a bad Christmas after all** January retail sales surprised, rising modestly at the headline and, excluding vehicles and gasoline, jumping 1.2% at the core level. The third biggest increase in core sales in this expansion wasn't enough to reverse December's bigger drop—core sales fell that month by the most since December 2000. But it did suggest consumer spending will remain supportive, a view reinforced by robust University of Michigan and Bloomberg consumer sentiment surveys.
- **Has housing turned the corner?** While the monthly sales rate slipped in January, big upward revisions to prior months put new homes sales on a rising trend, adding to evidence (builder confidence, starts, etc.) that housing may be accretive to growth this year. Builders were unable to keep up with demand as the stock of unsold homes fell, a function of improving affordability on rising incomes and moderating mortgage rates and home prices.
- **Prices support Fed patience** February's trio of price reports (consumer, producer and import) signaled moderating inflation, with year-over-year (y/y) producer and consumer prices rising at their slowest pace since June 2017 and November 2016, respectively. Y/y import prices fell a third straight month.

NEGATIVES

- **Soft landing watch** Industrial production rose less-than-expected in February and would have declined had it not been for a weather-related boost for utilities. The manufacturing component contracted a second straight month, and an early read on March based on New York's Empire gauge suggests factories remain under pressure. One bright spot was January's increase in nondefense capital goods orders, which climbed the most in six months, a sign capital expenditures (capex) have some momentum (*more below*).

- **Soft landing watch** The National Federation of Independent Business monthly survey of small business optimism rose in February for the first time in six months. But the meager increase was far short of expectations, keeping y/y momentum negative—a trend historically associated with slower growth.
- **China soft landing watch** China data continues to disappoint, as February industrial production hit a 17-year low. However, March exports are tracking at about a 40% y/y increase, suggesting early-year weakness may be a function of the Chinese New Year holiday distortions and not incremental underlying weakness.

WHAT ELSE

Dot.com redux? Empirical Research says today's valuation paradigm, with high P/E-multiple growth stocks driving performance, is virtually identical to that of March 1999, a year before the historic top of the dot.com era. Technology adoption cycles, driven by price deflation, underpinned both episodes. The market has a habit of stymieing as many people as possible, particularly late in a cycle, and that may again prove to be the case.

We are betting on capex If capex growth is about to slow, it was not apparent in the Q4 GDP report. Real nonresidential fixed investment surged 6.7% y/y, its fastest pace in more than four years. Nominal capex grew at a robust 8.6% rate, led by a 12.6% jump in research & development and a 12.3% jump in software spending. The sustainability of capex momentum may be the most important factor impacting growth in 2019 and beyond.

Not everything is a lie One of the greatest misconceptions in the public discourse surrounding corporate buybacks is the belief managements repurchase stock to try and inflate earnings per share (EPS) and meet incentive compensation targets. Goldman Sachs research shows that executives whose compensation depends on EPS—a metric that would benefit from accretive share buybacks—did not allocate a higher proportion of 2018 total cash spending to buybacks than companies where management pay is not linked to EPS.

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DISCLOSURES

Views are as of the date above and are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector.

Beta is a measure of the volatility, or systematic risk, of a security or a portfolio, in comparison to the market as a whole.

Gross Domestic Product (GDP) is a broad measure of the economy that measures the retail value of goods and services produced in a country.

Price-earnings multiples (P/E) reflect the ratio of stock prices to per-share common earnings. The lower the number, the lower the price of stocks relative to earnings.

S&P 500 Index: An unmanaged capitalization-weighted index of 500 stocks designated to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Indexes are unmanaged and investments cannot be made in an index.

The Empire State Manufacturing Index gauges the level of activity and expectations for the future among manufacturers in New York.

The New York Stock Exchange (NYSE) advance/decline line measures the ratio of advancing stocks to declining stocks.

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